

July 2016 | [ey.com/dde](http://ey.com/dde)

Digital Deal Economy Study

# Dealing in a digital world

Capital strategies to future-proof  
your business





Building a better  
working world

Grow your own? ☐

Buy? ☐

M&A can offer a faster route to digital than organic growth. Acquiring innovation could transform your business. [ey.com/tas](https://ey.com/tas)



The better the question. The better the answer. The better the world works.

# Dealing in a digital world



**Steve Krouskos**

Global Vice Chair  
Transaction Advisory  
Services

The business world is being transformed. Advances in technology and digital communications have not only empowered customers but also enabled companies to collect, collate and analyze data in new ways that better inform strategic decisions and change how they operate.

Executives recognize that digital transformation is impacting all aspects of their business – from the front - end to the back. They also know that the competitive landscape is changing rapidly as barriers to entry are eroded. Our study finds 90% of executives facing increased competition from companies that have been quicker to embrace digital.

Enabling a digital future requires smart capital allocation. Selecting the right strategic investments – organic or inorganic – offers routes to growth. The key question is can companies build the capabilities required to succeed in the brave new world – or do they need to buy?

According to our survey, 67% of respondents see M&A as the most efficient way to get there – acquiring digital capabilities, assets and technologies to bridge gaps and accelerate growth. A similar number say a rapid response is essential.

However, buying has significant challenges. The digital deal environment is becoming intensely competitive. The rise in acquisitions is not only coming from technology companies buying within the industry, but also from strategic buyers of all types as sectors blur. At the same time, considerations underpinning a deal are becoming more challenging – from the valuation of nonphysical digital assets to the integration of new entrepreneurial cultures into traditional company models.

Other inorganic routes also offer options. Companies are increasingly employing smart collaboration including alliances, partnerships and joint ventures, throughout their value chain. This enables companies to fast-track the build-out of their digital capabilities to remain competitive.

Ultimately, achieving digital transformation involves strategic questions that are many and highly complex. What to buy? Whom to partner with? How to fund ongoing investment?

Our report provides insights to help businesses – whether they are in the early stage of a digital transformation or further down the track. Our findings demonstrate that the most effective way to navigate this journey is to make investment decisions that support the future vision for the digitally enabled business. A future-proofed digital capital strategy is at the heart of dealing in a digital world.

## About our study



The Digital Deal Economy Study focuses on the impact of digitalization on business and on strategic options to transform business models and operational processes.

The results of the 2016 survey, on which the study is based, come from more than 600 interviews with non-technology corporate executives – mostly from large companies. The research was conducted in March 2016 by FT Remark, the research and publishing arm of the Financial Times Group.

- ▶ Seventy percent of respondents are from companies with revenues of over US\$5b.
- ▶ Executives are from companies across the Americas, Asia-Pacific, Europe, the Middle East, India and Africa.
- ▶ Equal proportions of executives describe themselves as strategy and technology leaders.
- ▶ Eight industry sectors are represented: agribusiness, automotive, consumer products, financial services, life sciences, media and entertainment, oil and gas, power and utilities.
- ▶ Sixty-one percent of all respondents have completed more than one acquisition in the past two years.



**Tony Qui**  
Chief Global  
Digital Officer  
Transaction Advisory  
Services

### Digital defined

Digital is a continuous form of disruption to existing (or new) business models, products, services or experiences, enabled by data and technology across the enterprise.

The key challenge for many companies will be a lack of sufficient capital to meet their digital ambition.

## Over the past two decades, companies have ramped up their technology, many without a coherent digital strategy, in an effort to keep up with the relentless pace of digitalization

Today's fast-moving and increasingly disruptive technologies are adding to the pressure, resulting in competitive advantage for those companies that are quickest to adapt, blurring the lines between sectors and allowing new entrants to introduce collaborative business models that break all the rules. Companies struggling to keep pace are feeling the effects on their margins and their ability to survive.

EY surveyed 600 non-tech corporate executives from around the world about their digital strategies and have distilled their answers down to these key findings:

### The digital future is here

Today's digitally transformed world is introducing new and unpredictable competitive pressures that businesses need to address if they want to survive and thrive. Our survey found that 90% of businesses are facing increased competition from companies that have embraced digital, either existing competitors or new entrants.

### Capital is at the heart of an effective digital strategy

Eighty-five percent of respondents say they have an established digital transformation function in place as a focus for innovation. Digital is not an IT strategy or one-off investment. The scale of transformation needed requires a long-term capital strategy. The key challenge for many companies will be a lack of sufficient capital to meet their digital ambition. Businesses need to take a holistic view and incorporate their digital strategy into their "capital agenda" – an enterprise's strategy for capital allocation and confirm that leadership is committed in the long term to creating a digital mindset and a culture of agile innovation.

### Inorganic growth – the way forward

Organic digital initiatives can take years to reach the bottom line. M&A, joint ventures (JVs) and alliances provide the fastest strategic route to digital transformation and growth. Two-thirds (67%) of companies are planning to use M&A to upgrade their digital capabilities in the near future.

### Dealing in digital – the challenges

Our findings also reveal that most businesses rely on organic growth to fill their digital gaps. Integration (e.g, IP, systems, technology) and talent retention were major obstacles after the transaction had completed.

By developing an effective digital Capital Agenda, businesses will be in a better position to make the right investment choices. Considering digital strategy as a key component of capital allocation will support the business to transform and grow. M&A, JVs and alliances, alongside organic investment, can help build the innovation pipeline and effectively enable you to survive and thrive in the new digital world.



# The digital picture

---



## The impact of digital transformation

**76%**

say the most important element for a successful digital strategy is strategic vision mapped to digital needs

**74%**

say digital transformation has a substantial or transformative impact on how they conduct business operations and processes

**90%**

are facing increased competition from companies that have embraced digital

---



## How much capital is needed

**59%**

say digital is embedded in major decisions

**87%**

are explicitly considering digital transformation needs in capital allocation planning for the next two to three years

**55%**

have a sophisticated quantification of the capital needed to pursue digital

---



## Buy or build?

**59%**

don't have the in-house capabilities required to respond to digital transformation

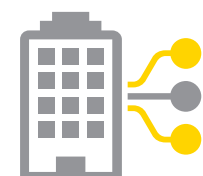
**68%**

say accelerating sector dynamics require a rapid response and an inorganic approach

**67%**

plan to use M&A to buy rather than build digital capability over the next two to three years

---



## Digital transformation function

**85%**

say they have established a digital transformation function

---

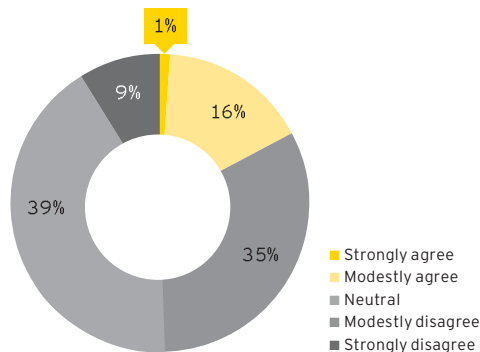
# The digital future is here

## Key questions:

- ▶ How is your business model being disrupted by digital?
- ▶ How could you leverage technology and digital capabilities to anticipate changing market behaviors?
- ▶ What are the strategic opportunities to digitize?
- ▶ Do you have the right capabilities in-house to achieve digital transformation?
- ▶ Can you monetize your data or build new services?

### Q: To what extent do you agree with the following statement?

Digital is having a minimal impact on our industry and we have no specific plans to address the issue.



Digital transformation was once all about the customer, from e-commerce to digital marketing. Customer service strategies focused on online interaction, online payments were introduced and marketing campaigns were tailored to a digitally native generation.

But now, 74% of respondents in our survey say digital has had a substantial or transformative effect on their business operations and processes, even more than on their relationships with customers (66%) and vendors and suppliers (59%). Just as pertinently, only 1% strongly believed that digital was having a minimal impact on their industry.

So, increasingly, companies are infusing digital innovation throughout the organization, shifting their focus from front-office customer concerns to back-end business matters and, indeed, the whole customer value chain.

Technologies such as the Internet of Things, artificial intelligence and big data, coupled with the ongoing growth in the creation and sharing of information, are changing the traditional business ecosystem in three distinct ways.

### Q: How would you characterize the extent to which digital transformation is impacting the following components of your business?

How you conduct business operations and processes (e.g., manufacturing, back office, talent management)



Your customer relationships (e.g., enhanced customer experiences, frequency of touch, more products/services, new transactional models, fulfillment ...)



Your relationship with vendors and suppliers (e.g., real-time ordering, just-in-time delivery, new transactional models, virtual fulfillment ...)



■ Transformative impact ■ Substantial impact ■ Moderate impact ■ Minimal impact ■ No impact at all

"To stay ahead of the competition, our company needs to disrupt traditional organizational structures, processes and systems. Mainstream business cannot continue with the status quo. We need to undergo significant change to fully integrate digital and other new technologies into all aspects of the business to deliver superior customer experience."

Senior vice president of finance, oil and gas company, Canada



**76%** say increasing competitive pressure is one of the biggest impacts of digital transformation on their industry



**95%** they are experiencing a degree of change in customer relationships due to digital



**76%** cite industry convergence as the biggest impact of digital transformation

### 1. New and unpredictable competitive pressures

As technology advances and new entrants compete for the digital customer base, companies will need to build distinctive business propositions and experiences to create new revenue streams. Ninety percent of respondents in our survey say they are facing greater competition from companies that have embraced digital, both old competitors and new entrants. Indeed, when it comes to new entrants to the market, one of the key factors is that digital start-ups now have almost instant access to millions of customers that traditional companies had the luxury of building up over many years. The barriers to entry have been broken down, and disruptors have the ability to scale up quickly.

### 2. Empowered customers

Greater access to information, via social media and growth of the mobile internet, is changing customer preferences and behaviors. Customers expect evermore personalized experiences, as well as greater engagement and convenience. And smart technology means that customers have the ability to transact at any time and from anywhere via their mobile device. As a consequence, 95% of executives say they are experiencing a degree of change in customer relationships due to digital, with 66% describing this as a substantial or transformative for their business.

### 3. Blurred industry boundaries

The digital revolution allows companies from different industries to challenge the dominance of leading players – 76% of our respondents cite this as the biggest impact of digital transformation. Driven by the need for growth among the tech giants, diversification is causing industry borders to blur and converge. From driverless cars to digital health care – the boundaries between traditional sectors are being broken down like never before. Today's leaders risk being toppled if they overlook shifts in the market, ignore new competitors and fail to innovate.

## Industry perspectives



Energy and mining



Power and utilities



Consumer products



Financial services



Life sciences



Automotive and transportation

### Biggest impact of digital transformation

Competitive pressures

Blurring boundaries

Competitive pressures

Blurring boundaries

Blurring boundaries

Competitive pressures

### Percentage that say they have clarity on the digital opportunities, risks and impact to the enterprise strategy

**53%**

**55%**

**76%**

**78%**

**59%**

**71%**

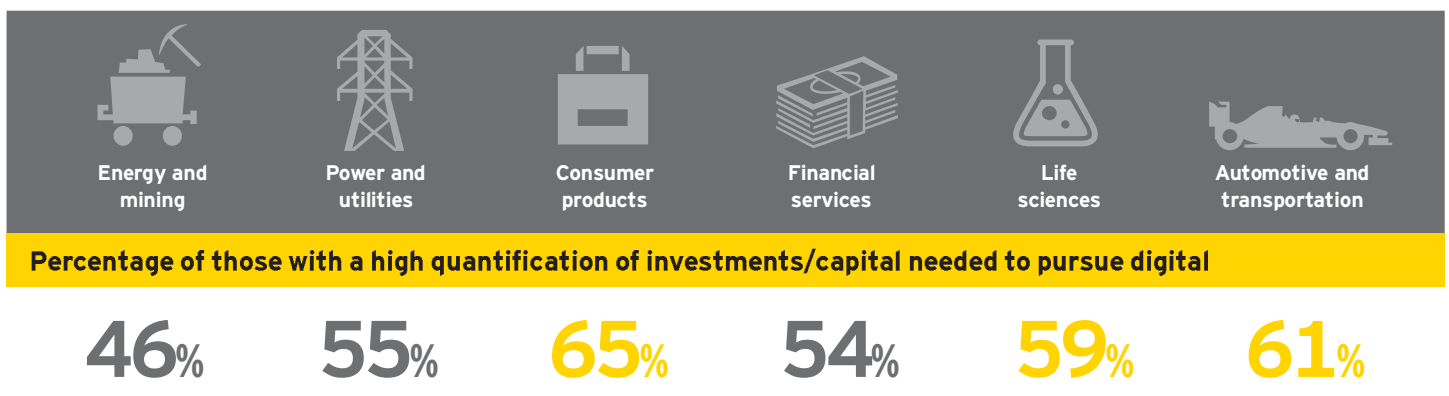
# Capital is at the heart of an effective digital strategy

## Key questions:

- ▶ What is the payback period for your digital and big data technology investments?
- ▶ How much of your digital strategy is supported by C-suite and shareholders?
- ▶ Do you understand where the gaps are in your portfolio, and how do you fill them?
- ▶ Do you have access to sufficient capital, or do you need to raise?

Successful digital transformation – one that produces growth and opens doors to new opportunities – requires a business model supported by an adaptable and agile capital strategy, driven by the C-suite. Most respondents say they have an established digital transformation function in place (85%) and understand that success means mapping their digital needs together with the company's vision (76%). In addition, 59% say digital is embedded in the major decisions they make.

## Industry perspectives





"The main elements in a digital transformation should include the board and management knowing — and being clear about — what they want; having the correct people to help them; and having the capital as well as the technology to bring in the changes."

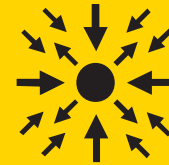
Chief financial officer, agribusiness, US



**76%** say a strategic vision mapped to digital needs is the most important part of digital transformation



**87%** are explicitly considering digital transformation in their capital allocation planning for the next two to three years



**55%** have a sophisticated method in place to quantify the capital needed

While it is evident that companies realize the importance of a digital strategy, one of the major challenges is that many of them, particularly those in more traditional sectors, are playing catch up and do not have a clear understanding of digital's role in their business. This leads to an inability to drive funding. So, while 87% of respondents in our survey say they are explicitly considering digital transformation needs in their capital allocation planning for the next two to three years, only 55% have a sophisticated method in place to quantify the capital needed to pursue digital transformation – and the results may be telling them that they do not have enough capital to do so.

#### Q: What are the key elements of executing a digital strategy successfully?

Clearly defined strategic vision mapped to an understanding of digital needs

76%

Sufficient IP/technology assets and proper integration into the business

60%

Involvement of appropriate digital expertise/experts

58%

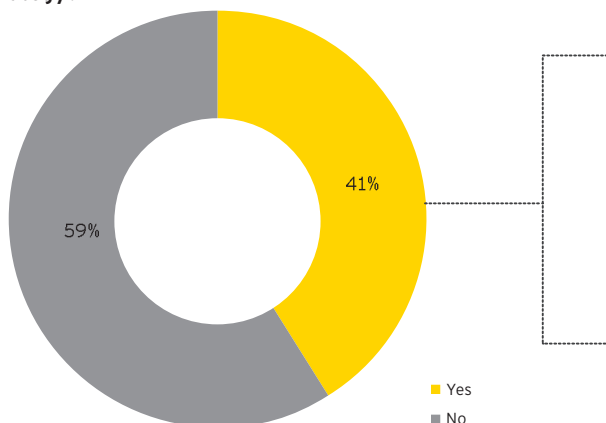
Having the required capital to be able to invest in digital

52%

Collaboration and alignment between M&A, digital and business unit teams

52%

#### Q: Are you considering divesting assets as part of your digital strategy?



#### Q: If you answered yes, what is the primary rationale?

Rebalancing your portfolio of assets

46%

Reshaping the core business

23%

Providing financing for new acquisitions

22%

Providing financing for internal R&D projects

9%

Capital is at the heart of an effective digital strategy

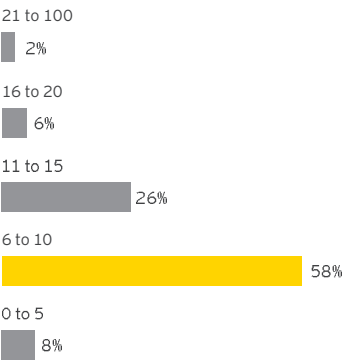


Capital is king

Digital is not a one-time investment, and appropriate funding is paramount. Yet our findings reveal that most businesses still rely too heavily on organic growth to build their digital capabilities. This is more than likely due to constraints on capital; indeed, nearly two-thirds of respondents (64%) stated they would only be allocating up to 10% of their capital budget on digital in the next two to three years.

This lack of capital is constraining growth. Many companies are not thinking about the disruptive forces at play. Capital management and digital strategy are often misaligned. Companies need to embed a digital strategy in their Capital Agenda (the strategic priorities assigned to the life cycle of their capital). A digital Capital Agenda that is also robust will help prioritize investment, and provide the sustained spending on digital needed to drive long-term growth. To that end, companies need to explore alternative capital-raising strategies, potentially through IPOs, alliances or rebalancing their existing portfolios via divestments.

Q: What percentage of your capital budget will be allocated to digital?



Buy or build? Do both

To successfully drive a digital transformation, companies need to review their current portfolio to understand gaps and combine inorganic M&A strategies or alliances with their organic investment plans. And to do that effectively, businesses need the capital. Those companies that are too capital constrained to undertake traditional M&A will need to broker alliances and partnerships to drive the new digital world. And these will not just be with vendors and suppliers, but also competitors.

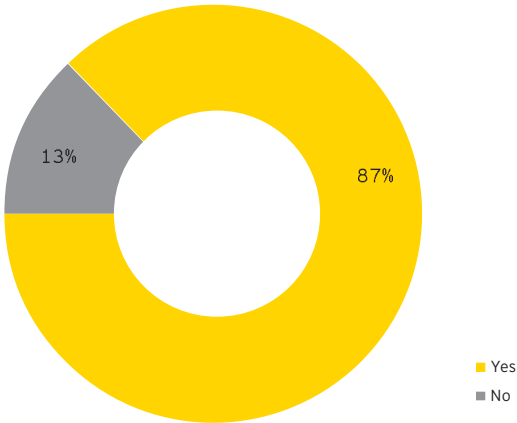
Those who choose to build through internally driven, organic initiatives will need strong in-house innovation capabilities to rival the nimblest start-up. Should internal technology officers be more comfortable at a slower pace, the company can consider a bi-modal approach: maintaining a traditional IT office, alongside an entrepreneurial IT-innovation team.

Who is executing the strategy?

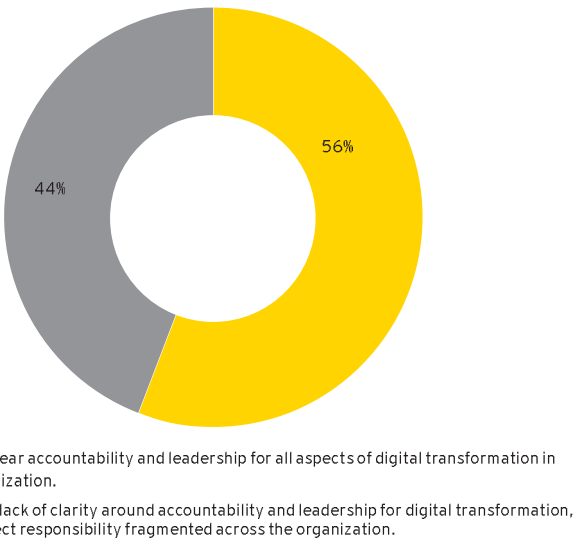
The lack of understanding around digital can lead to a lack of leadership focus, and this can muddy the digital transformation waters and limit the effectiveness of any digital strategy. A significant number of respondents (44%) report a lack of clarity around accountability when it comes to the digital transformation process, with responsibility fragmented across the organization. Our survey reveals that clarity is desperately needed around ownership and accountability.

Even those with clear accountability view their digital strategy to be the responsibility of several executives. Few respondents see the CEO or even the CFO as responsible for the strategic aspects of digital transformation. Instead, the chief digital officer, the chief technology officer (or similar) or the chief marketing officer are most often identified as being responsible, while the board and the shareholders are cited as the real decision-makers. It is unlikely that these various roles will produce a coherent picture needed to implement a successful front- and back-end transformation. Digital strategy drives capital allocation, and businesses need to be crystal clear on who is allocating that capital.

Q: Are you explicitly considering digital transformation needs in your capital allocation planning for the next two to three years?

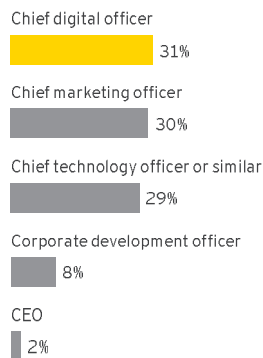


Q: Which of the following statements best characterizes your organization's approach to decision-making and accountability?

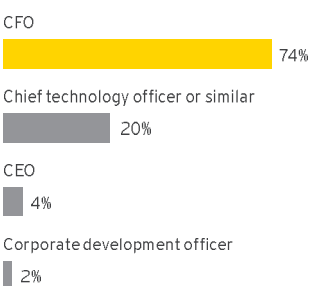


Q: If there is clear accountability in your company, who is responsible for the primary aspects of digital transformation?

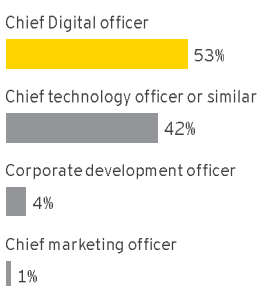
Strategy



Funding



Implementation





# Inorganic growth – the way forward?

## Key questions:

- ▶ What is the best way for you to build innovative capabilities and culture?
- ▶ Should you develop in-house capabilities further or buy them?
- ▶ Do you know where assets and capabilities needed are located and/or available?
- ▶ Do you know how to find attractive assets, partnerships and alliances?
- ▶ How do you protect and realize value once you have acquired the companies?

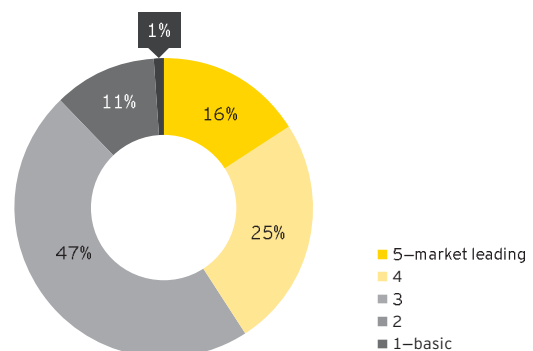
While the majority of respondents stated that they are relying on organic growth to fill their digital gaps, it is telling that 59% revealed that they do not have the in-house capabilities required to respond to digital transformation.

Organic digital initiatives can take years to reach the bottom line. M&A, JVs and alliances provide the fastest strategic route to digital transformation and growth.

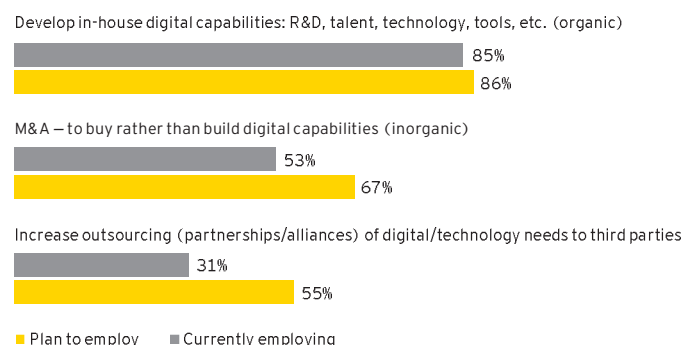
In the face of rapidly accelerating change, our findings reveal that more companies are turning to M&A, partnerships and alliances. Two-thirds (67%) of companies are planning to use M&A to upgrade their digital capabilities in the near future, up from the 53%.

In our survey, 90% of respondents are facing increased competition from companies that have embraced digital. Of those, 62% said those rivals had reached their competitive position inorganically. However, only 48% of respondents have themselves completed acquisitions in the past two years that were designed to support their own digital transformation. Again, an effective digital strategy underpinned by a digital Capital Agenda will help enable innovation.

**Q: How would you rate your organization in terms of its approach/response to digital transformation on a scale of 1-5?**



**Q: Which of the following strategies are you employing, or plan to employ, to address your digital transformation needs?**





"It's cheaper and more efficient for our company to buy rather than build. We are able to acquire technologies that are new to us and that we would not be able to build or develop on our own."

Chief innovation officer, life sciences, US

## What companies have acquired and what they want to acquire

In the past, the majority of companies have focused on buying customer-facing and advertising/marketing technologies (34% and 32%, respectively). However, both of these are set to fall in the future.

The key growth areas in terms of acquisitions are analytics and cybersecurity. In past deals, only 20% of respondents were concentrating on these subsectors – this rises to 27% in terms of future deals. Yet, despite this growth, analytics and cybersecurity are still the smallest proportion of all the capabilities that companies are looking to buy.

It would appear that, as companies become more comfortable with technology and progress, their digital strategy, in line with industry innovation capabilities such as payment and processing solutions and 3D printing solutions, will grow.

However, much of this is evolutionary as opposed to revolutionary technology. As digital strategies progress, companies need to ensure they are allocating capital for the next wave of innovation, such as robotics and artificial intelligence.

## Q: What capabilities did you acquire and, as part of your company's digital transformation strategy, which are the main capabilities you are looking to acquire?

Routes to customer segments, customer identification and conversion



Advertising and marketing technologies



Payment and processing technology



Distribution and 3D printing solutions

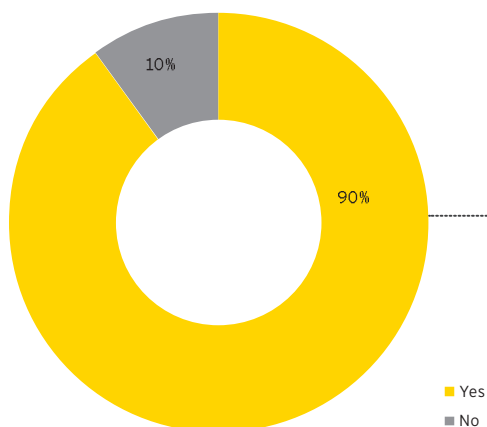


Analytics and cyber solutions

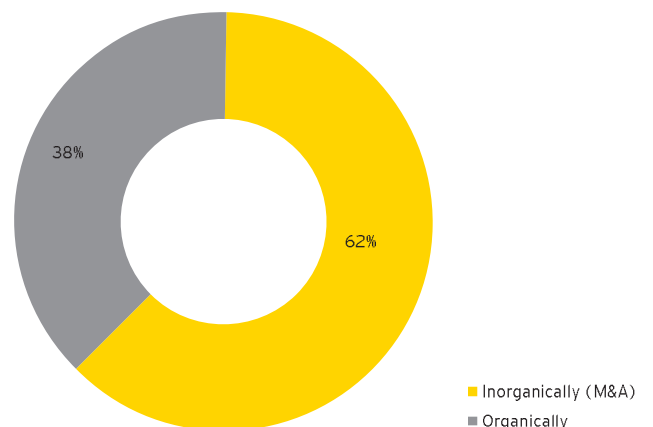



■ Future ■ Past

## Q: Are you facing increased competition from companies that have embraced digital?



## Q: If you answered yes, how have they reached their competitive position?





## Inorganic growth – the way forward?

### Agile alliances

As companies look for new digital capabilities, alliances – in addition to and sometimes in place of acquisitions – are also proving attractive. A third (32%) of respondents plan to create alliances and partnerships in the next two to three years.

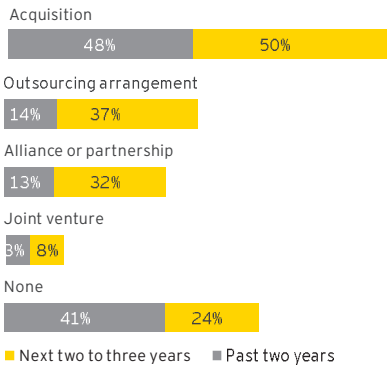
Unlike joint ventures, alliances are usually less involved and not permanent, offering greater flexibility to businesses pursuing a digital transformation strategy. Alliances allow companies to plan for multiple futures. Companies can commit underused assets, or assets that others are better positioned to exploit, in exchange for more efficient digital capabilities owned by collaboration partners. An effective strategic alliance will allow each company to maintain its autonomy while discovering new opportunities and more effective processes, as well as access to new markets.

Companies are increasingly leveraging alliances with clients, suppliers, vendors and institutions to create new business models and ecosystems, increasing operational efficiency and integrating the whole value chain to better serve the market, while also increasing competitiveness. Swift-footed companies are investing in promising start-ups via incubations, collaborations and sponsorships and integrating them to provide cutting-edge digital services.

However, while the benefits of alliances or JVs are evident, companies need to ask themselves six key questions before embarking on these partnerships:

- ▶ Who are suitable targets and how do you value them?
- ▶ If you are creating an alliance or JV, how do you profit from it?
- ▶ If your alliance creates joint intellectual property (IP), who actually owns that IP?
- ▶ How do protect your IP?
- ▶ What is the best way of forming an alliance to protect value?
- ▶ How do you protect your customers and their data?

**Q: Which of the following has your company undertaken in the past two years, and which will they undertake in the next two to three years to achieve its digital transformation goals?**



"Our rationale behind creating an alliance with a third party was to gain advanced technological aptitude. Our partners possess technology expertise encompassing a wide range of industries and geographies that has helped us expand our global reach and create further efficiencies in our supply chain and other operations."

Global director of marketing, life sciences, Denmark

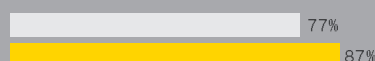
## Industry perspectives

### Build, buy or ally?

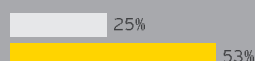


#### Energy and mining

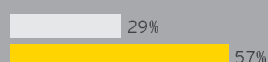
Develop in-house digital capabilities: R&D, talent, technology, tools, etc. (organic)



M&A – to buy rather than build digital capabilities (inorganic)



Increase outsourcing (partnerships/alliances) of digital/technology needs to third parties

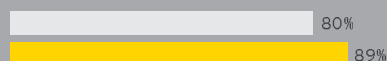


Even though commodities prices remain volatile, respondents are looking to increase each aspect of their digital capital allocation strategy. M&A is set to grow by 28 percentage points – albeit from a lower level than other sectors.

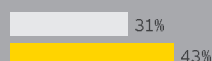


#### Power and utilities

Develop in-house digital capabilities: R&D, talent, technology, tools, etc. (organic)



M&A – to buy rather than build digital capabilities (inorganic)



Increase outsourcing (partnerships/alliances) of digital/technology needs to third parties

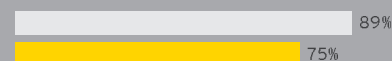


The power and utilities industry is set to grow each aspect of its digital capital allocation strategy in the coming years. While inorganic growth remains high, companies seem keener on alliances and partnerships than traditional M&A.



#### Consumer products

Develop in-house digital capabilities: R&D, talent, technology, tools, etc. (organic)



M&A – to buy rather than build digital capabilities (inorganic)



Increase outsourcing (partnerships/alliances) of digital/technology needs to third parties

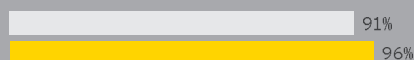


There is a significant drop-off in the development of in-house capabilities for consumer products companies – 14 percentage points. This will be replaced by increasing levels of M&A and partnerships or alliances.

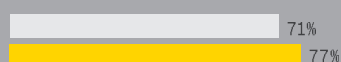


#### Financial services

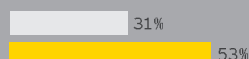
Develop in-house digital capabilities: R&D, talent, technology, tools, etc. (organic)



M&A – to buy rather than build digital capabilities (inorganic)



Increase outsourcing (partnerships/alliances) of digital/technology needs to third parties

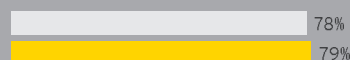


The rise of FinTech means that financial services groups need to be laser-focused on their digital strategy. To that end, M&A will increase from an already high starting point, while alliances are set to expand by 22 percentage points.

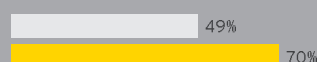


#### Life sciences

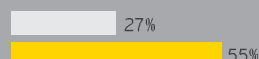
Develop in-house digital capabilities: R&D, talent, technology, tools, etc. (organic)



M&A – to buy rather than build digital capabilities (inorganic)



Increase outsourcing (partnerships/alliances) of digital/technology needs to third parties



As digital health care becomes mainstream, life sciences companies are set to respond by significantly upping their levels of M&A and brokering more alliances and joint ventures with digital partners.



#### Automotive and transportation

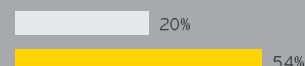
Develop in-house digital capabilities: R&D, talent, technology, tools, etc. (organic)



M&A – to buy rather than build digital capabilities (inorganic)



Increase outsourcing (partnerships/alliances) of digital/technology needs to third parties



The advent of technologies such as driverless cars and ride sharing has swiftly turned the automotive industry into the mobility business. Companies will meet the increased digital demands via M&A and significantly more partnerships.

■ Future ■ Current



# Dealing in digital – the challenges

## Key questions:

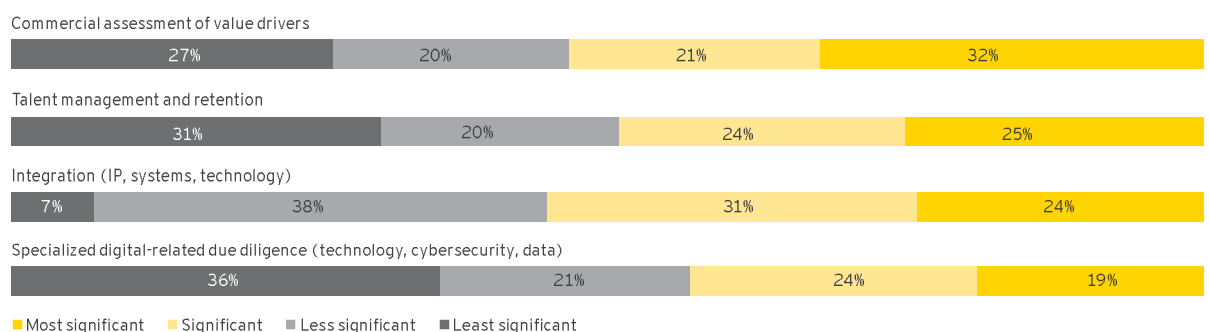
- ▶ How will you value assets and capabilities?
- ▶ How will you assess cyber risks related to a proposed deal?
- ▶ How will you integrate acquired digital capabilities into your current business?

From assessing value drivers to due diligence, there are challenges that need to be addressed when dealing with M&A driven by digital transformation.

Respondents highlighted a number of particular challenges when buying digital capabilities, including integration (e.g., IP, systems, technology), talent management and retention, and the commercial assessment of value drivers.

Moreover, the rise in acquisitions has not just come from technology companies buying within the sector, but from strategic buyers of all types – many of whom will not have the knowledge base to deal with challenges that are specific to technology transactions.

## Q: What were the most significant challenges that you encountered in your last digital transformation-driven acquisition?





# 1

## Value and new due diligence

Valuing digital targets – some of which will be pre-customer, pre-revenue and pre-profit – can be as much art as science. Good data is essential to build buyer confidence and allows a better assessment of the value of capabilities acquired.

However, specialized digital-related due diligence (including technology, IP valuations, cybersecurity, social media and data analytics) was the fourth most significant challenge cited in our survey. When buying a start-up or a fast-growing tech business, the due diligence demands can be very different. Due to the competitive nature of the industry and the pace of change, these innovative companies are snapped up swiftly. Bidders need to change their due diligence process to match the market.

The ability to quickly and efficiently analyze the vast amount of data at a company's disposal will have a dramatic effect on dealmaking. Acquirers need more sophisticated and powerful processes for identifying, approaching and screening opportunities. Working with the right advisor can play a pivotal role in understanding and realizing value from a transaction, while also reducing risks.

# 2

## Taking on talent

Similar risks and clashes can occur when it comes to a target's people and culture, especially when acquiring start-ups. For acquirers, balancing the founder's need for entrepreneurial autonomy with the incumbent's established processes can be a major challenge. Further, major corporations and start-ups have different attitudes to the treatment of talent – the very talent you are hoping to retain for your digital strategy.

Acquirers should identify key people early in the deal process and work to win their engagement and build trust. If there is outstanding talent in the target company, offering them larger roles in the organization can be motivational. Tie-in periods can show the benefits of being part of a larger entity.

If designed well, retention agreements can buy time to engage talent, articulate what they are going to do and really live it so that people are deeply ingrained in the organization and want to stay beyond the agreed time. Companies need to ask themselves how they can motivate and use the talent team as a catalyst to spark the leadership team into action.

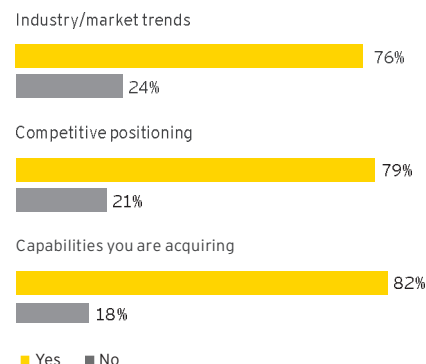
# 3

## Integration issues

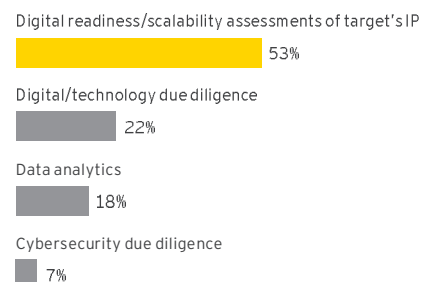
Post-deal integration, IP, systems and technology must be carefully addressed. More than half (55%) of respondents highlight integration as a significant challenge. Yet, only 37% of respondents to our survey have a different integration strategy for digital transactions. In addition to technological legacy concerns and compatibility issues, regulation and competition law could be an issue. When acquiring a cloud-based business, for example, there may be risks associated with its use of technology depending on the market, which can complicate a deal.

In order to protect investment, buyers need to have a different approach to integration. This could be a tri-modal model: keeping the incumbent business ticking, incentivizing everyone on the innovation group, and buying a new business and keeping it separate. Some companies may not be mature enough to integrate.

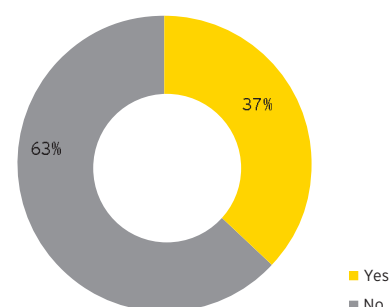
**Q: For your digital transactions, do you undertake front-end strategic pre-deal analysis of the digital landscape to understand the following?**



**Q: In your most recent transaction, did you incorporate any of the following into the deal process?**



**Q: Do you have a deliberate integration strategy for digital transactions that differs from "traditional" transactions?**



### Digital – defining a new normal for M&A

The entire process of deal-making is being transformed. Increased competitive intelligence and better opportunity analysis are required to spot and make the right deal in today's complex marketplace. In the face of quick-footed competitors, the pressure is on to keep pace and make capital decisions around acquisitions, alliances and JVs quickly. Companies need to be more proactive in terms of pipeline management and deal origination, dedicating more internal resources and time than they did in the past to identify the right targets. They now have to evaluate potential acquisitions much earlier, long before the actual transaction. Corporate development functions will need to be able to use advanced analytics of big data, mining vast amounts of structured and unstructured information and turning that into a commercial advantage.

New ways of measuring performance through diligence – social media diligence, for example – will help determine whether assets fit the strategy or help change the strategic direction of a business.

Evaluating a company's digital readiness is now crucial in a transaction. If a potential target company is not set up to adapt to digital disruption, then it will be complicated to try and bring it into a business that's already digitally focused. The question you should be asking is "How well does it fit into my ecosystem?"

# How EY can help

## The Digital Capital Agenda

Your capital strategy in a digital world should look to gain competitive advantage through organic and inorganic/M&A routes to growth. Acquisitions are a potential route to growth as acquired technology platforms, start-up businesses and innovation could transform your business. Divestments offer the chance to reshape your business and enable you to reinvest in digital capabilities.

EY's Transaction Advisory Services Digital Capital Agenda helps businesses respond to digital disruption and realize strategic options by focusing on raising, preserving, investing and optimizing capital.



### Raising

- Identify funding options
- Assist in fundraising (equity and debt) and address capital markets requirements
- Advise on how to optimize funding/financing structures
- Identify assets and operations to divest
- Advise on tax-efficient structures, including challenges arising from new digital products



### Preserving

- Assist with digital improvement analyses – enterprise-wide or product
- Perform valuations to model the impact of digital alignment on company economics
- Analyze customers and suppliers via social media monitoring
- Help preserve tax assets and reduce costs
- Analyze customer journey (mobile, website, call center, email, social)



### Investing

- Advise on acquiring digital operations and services, including financial and tax-related matters
- Provide digital commerce due diligence and growth strategy analyses
- Evaluate the infrastructure and digital capabilities underlying investment decisions
- Perform transaction diligence, including digital analyses aimed at revenues and costs
- Advise regarding tax structuring, including consideration of digital models



### Optimizing

- Develop strategy and business models to improve a company's digital positioning
- Assist with digital scenario planning and assess impact to shareholder value
- Identify and evaluate assets
- Support operational reorganization through modeling, planning and implementation to improve a company's digital value

Evidence from this study clearly shows that companies should no longer only pursue organic R&D activities to meet their digital ambition. With limited capital and time, companies should look to create a balance using M&A, JVs and alliances to ensure their survival.



**For a conversation about your capital strategy, please contact us.**

**Global  
Steve Krouskos**

EY Global Vice Chair  
Transaction Advisory Services  
@SteveKrouskos  
steve.krouskos@uk.ey.com  
+44 20 7980 0346

**Julie Hood**

EY Deputy Global Vice Chair  
Transaction Advisory Services  
julie.hood@au.ey.com  
+61 3 8650 7496

**Tony Qui**

EY Chief Global Digital Officer  
Transaction Advisory Services  
tqui@uk.ey.com  
+44 20 7951 5820

**Paul Macaluso**

EY Innovation Leader  
Transaction Advisory Services  
paul.macaluso@ey.com  
+1 213 240 7040

**Americas**

**Bill Casey**

EY Americas Leader  
Transaction Advisory Services  
william.casey@ey.com  
+1 305 415 1645

**Asia-Pacific**

**Harsha Basnayake**

EY Asia-Pacific Leader  
Transaction Advisory Services  
harsha.basnayake@sg.ey.com  
+65 6309 6741

**Europe, Middle East, India and  
Africa (EMEIA)**

**Andrea Guerzoni**

EY EMEIA Leader  
Transaction Advisory Services  
andrea.guerzoni@it.ey.com  
+39 028 066 9707

**Japan**

**Vince Smith**

EY Japan Leader  
Transaction Advisory Services  
vince.smith1@ey.com  
+ 81 3 4582 6400

EY | Assurance | Tax | Transactions | Advisory

About EY

EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. For more information about our organization, please visit ey.com.

About EY's Transaction Advisory Services

How you manage your capital agenda today will define your competitive position tomorrow. We work with clients to create social and economic value by helping them make better, more informed decisions about strategically managing capital and transactions in fast-changing markets. Whether you're preserving, optimizing, raising or investing capital, EY's Transaction Advisory Services combine a unique set of skills, insight and experience to deliver focused advice. We help you drive competitive advantage and increased returns through improved decisions across all aspects of your capital agenda.

©2016 EYGM Limited. All Rights Reserved. 1607-1978012  
EYG no. 01967-163Gbl

ED None

This material has been prepared for general informational purposes only and is not intended to be relied upon as accounting, tax or other professional advice. Please refer to your advisors for specific advice.

The views of third parties set out in this publication are not necessarily the views of the global EY organization or its member firms. Moreover, they should be seen in the context of the time they were made.