

The digitisation of everything

How organisations must adapt to
changing consumer behaviour

Digitisation is a step change even greater than the internet. Exponential technology advances, greater consumer power and increased competition mean all industries face the threat of commoditisation. The winners will act now, and build a strategic advantage that leaves their counterparts wondering what happened.



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The digitisation of everything

An imperative for digital innovation and engagement has emerged: businesses have already realised that they must use digital channels to engage with their key stakeholders to maintain relevance and drive the conversation. However, few realise how fast the change needs to happen, or how transformational it needs to be.

The real imperative in a world where 'everything' is digitised is that businesses need to pursue innovation to disrupt their own business model before the competition does. Without innovation strategies, companies will lose their competitive advantage in an increasingly commoditised world. There is no time to lose, as technology change accelerates exponentially and new digital platforms and devices are emerging. Furthermore, the expectations of the new 'generation Y' or 'digital natives' mean that companies must keep up with the pace of change or lose relevance.

The challenge for businesses is to **face the implications of digital change**: in particular, the loss of control over the customer relationship, increased competition and threat of commoditisation, and the need to engage digitally with suppliers, partners and employees in addition to customers.

The starting point is a structured approach to assessing your digital maturity based on an understanding not just of the technology, but of the 'big picture' of what digital engagement means to the business.

To deal with this challenge, companies must **develop an end-to-end response**. They need to develop a comprehensive digital strategy and rethink their business and operating models to deliver this. Such a strategy must go far beyond the Marketing department: it has to be about ubiquitous cross-channel connectivity, it must enable continuous engagement with customers, suppliers, employees and investors. It must also be about C-Level leadership, and critically it must be about innovation and differentiation through the business/operating model.





The issue

The imperative for digital engagement

Defining 'digital'

Digitisation at its simplest means the conversion of analogue information into digital information. As digitisation capabilities extend, virtually every aspect of life is captured and stored in some digital form, and we move closer towards the networked interconnection of everyday objects. The impact of this is a real-time global exchange of information between multiple connected devices (fixed and mobile).

Businesses must use digital channels to create seamless and consistent engagement

With the introduction of the first commonly used commercial websites in the 1990s, digital technology brought a new level of convenience to customers. However, digital convenience came at the expense of meaningful engagement as digital transactions substituted physical interactions. In addition, digital channels develop in isolation, resulting in inconsistency and dislocation between digital and physical channels. The legacy is one of frustration for today's customers, when for example they find they cannot complete an interaction they began online when they walk into the store. The frustration is particularly felt by digital natives who have grown up used to immediacy and convenience and expect to be 'known' at every interaction with a company, regardless of the channel in which they choose to engage. Now, however, new technologies exist (see figure 1) that make it easier than ever before for companies to bring channels together, and to deliver a consistent engagement model whether customers choose to 'tweet' or to take their feet to the street.

Innovative companies are taking the elements of each channel that their customers value most, and combining them to deliver a more valuable experience overall. For example, fashion retailer All Saints has integrated the convenience of web browsing in their physical stores by adding internet enabled kiosks on-site, so customers can browse and check availability on-line, and then try the item on in-store and get the best of both worlds. Apple stores use mobile Point of Sale terminals to add the convenience of 'click to pay' to their physical shopping experience and provide customers with an email receipt from the POS terminal.

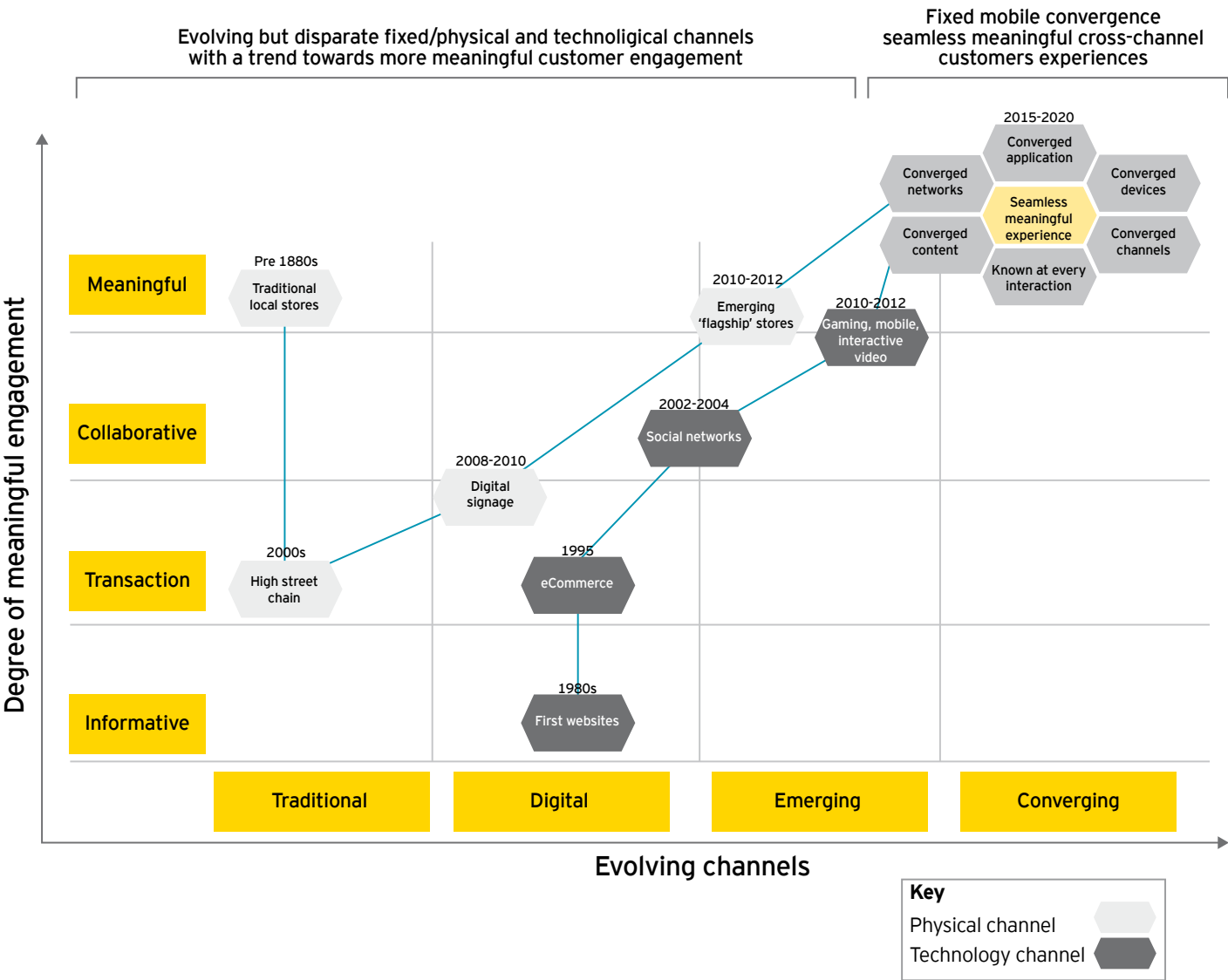
Organisations must focus on delivering a seamless and meaningful cross-channel engagement model for their stakeholders. Figure 2 shows how the engagement model has changed to date, and how it may evolve in the future. To get this right will require an agile strategy that means incorporating the latest technology as it is released, and adopting a test and learn approach. Companies should adopt a continuous improvement strategy, launching new digital channels early and iterating based on customer feedback.

Figure 1: How emerging technologies can be used for physical/digital channel integration

Example technology	Use for channel integration
<i>Location based services</i>	Services to digitally identify a physical location of a person or object (e.g nearest ATM). Also used to replace coupons for advertising to customers based on their actual physical location
<i>QR coding</i>	Allows users to scan a physical object (paper or building wall) and access further information in a digital fashion on their mobile
<i>Augmented reality</i>	Information about the surrounding real world of the user becomes interactive when viewed through a digital screen. Often used to make sports spectatorship interactive.
<i>Electronic paper</i>	A computer that feels and operates like a thin sheet of paper which can interpret text written directly onto it



Figure 2: How engagement is changing over time (Source: Ernst & Young research)



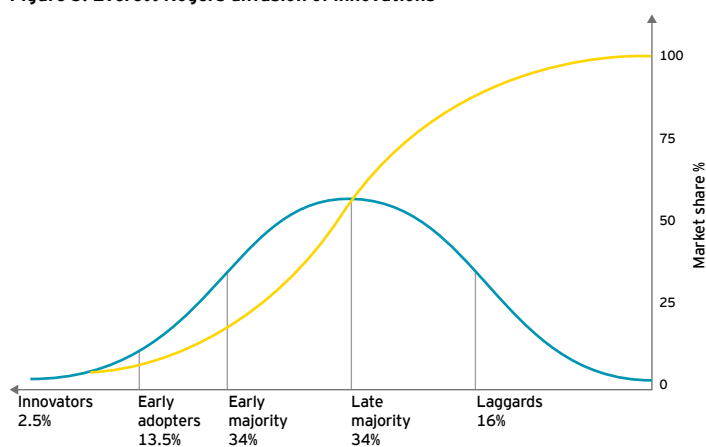


The pace of technology change is increasing exponentially

Most companies understand the need to respond and adapt to the evolving use of technology by their customers and other key stakeholders. What they do not realise is how little time they have to address these changes.

Technology adoption typically occurs in an S-curve, with exponential growth of technology adoption from 'early adopters'. Not only is the diffusion of individual technologies exponential, but the rate of diffusion is accelerating, and with each new technology release, the 'early adopters' and 'early majority' move further to the left. It took more than 70 years for telephones to reach 50% household penetration, compared with 28 years for radio, and 10 for internet access¹. Following this trend, the rate of technology adoption should continue to accelerate so that each new technology outpaces the adoption of its predecessor, and the future will see adoption rates measured in weeks and days rather than years. Google+, the new social media tool from Google took only 16 days to reach 10 million users, compared with 780 days for Twitter and 852 days for Facebook. It took 10 years for the internet to become a basic and essential part of daily life. The future will happen much faster than that.

Figure 3: Everett Rogers diffusion of innovations



The rapidly advancing price/performance capability of computing, storage, and bandwidth is contributing to an adoption rate for the digital infrastructure that is two to five times faster than previous infrastructures, such as electricity and telephone networks². By 2020 there will be 50bn internet enabled devices³. Those 50bn devices will become interconnected into a web of the 'internet of things' and could include fridges that can replenish themselves by ordering from the supermarket, and other devices associated with the 'intelligent home'. In amongst the new devices will also be disruptive technologies such as Electronic Paper which can be folded and carried in a pocket, and may drastically change the future of printing and other industries.

The proliferation of digital channels, platforms and devices has produced a generation who are born 'plugged-in'⁴. This 'Generation Y' already plays a major role in accelerating the emergence of a new, digital world, and their impact is impossible to ignore. Generation Y's expectations are being formed by the technologies they surround themselves with. They adapt their lifestyles to each new technological invention and they won't accept that the brands they interact with or employers they work for don't do the same. Generation Y already constitutes a new category of consumers, citizens and employees who are digitally, globally and constantly connected. They are networked, collaborative and highly social. It is also Generation Y who are inventing the disruptive business models that challenge the status quo of existing organisations, as Mark Zuckerberg did with the invention of Facebook. In this way they are determining the way digital communication technologies are being used, and are initiating social behaviours that are transmitted to other generations.

“Digital natives were all born after 1980 when social digital technologies became widely used; they all have access to networked digital technologies and they have the skills to use these.”

John Palfrey and Uri Gasse, 'Born Digital'

Generation Y: Expectations and influence

Organisations that have succeeded in engaging with Generation Y know that, as well as accelerating the take-up of new digital technology, this generation poses additional challenges due to their evolving expectations. Generation Y are best thought of not as a uniform group but as an evolving mindset, and the demands and expectations of this group are trending upwards to older generations, which makes them all the more important to take note of. They are today the catalysts and the incubators of change, but each day their influence is growing in consumer and corporate environments, meaning that organisations must learn to engage effectively now, or risk being shut out of the game.

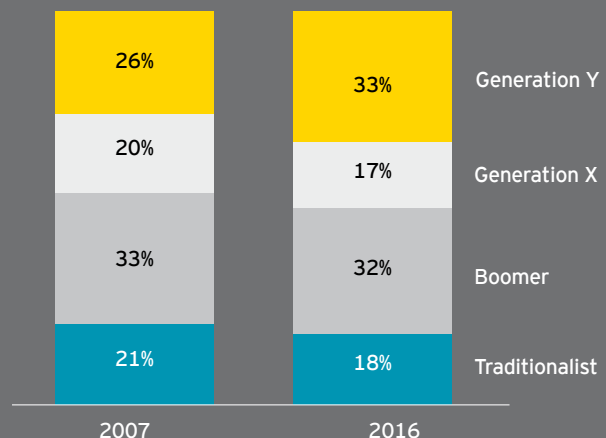
To attract these young people, both as consumers and as employees, a company cannot just look good – it has to be good. Generation Y want it all, but above all they seek transparency. It is no longer possible to say one thing and be another, as the digital data trail means the new generation has the tools and methods to spread their opinion about a brand virally, and with untold consequences. This has significant implications for brand reputation management and customer loyalty. Generation Y want to ensure that the organisations they engage with are authentic and not a hologram or mirage with a marketing 'front' that belies their reality. Authentic, direct and personal engagements are even more important than advertising to reach this generation.

Above all, Generation Y are no longer content with the old corporate and political model. They seek transformational change, and where they cannot find it, they look to invent it themselves. Figure 4 shows a handful of the most significant digital business model inventions of the last decade and the young minds behind these.

Figure 4: The young minds behind digital business model innovation (Ernst & Young research)

Digital Business Model	Creator/inventor	Year of birth
Facebook – social networking	Mark Zuckerberg	1984
Napster – peer to peer file sharing	Sean Parker	1979
Spotify – digital music streaming	Daniel Ek	1983
Skype – VOIP telephone network	Janus Friis	1976
Twitter – microblogging social network	Jack Dorsey	1976

Figure 5: Changing demographics (source: Ernst & Young Research)



According to our research, other Generation Y expectations include:

- ▶ Collaborative, networked learning: the average user spends 55 minutes a day on Facebook
- ▶ Fast, easy and fun communication: Generation Y adults spend 15+ hours a week on the internet
- ▶ Visible peer recommendations in decision-making: 80% of consumers believe peer recommendations, but only 14% trust advertisements
- ▶ Immediate feedback: 34% of bloggers post opinions about products and brands
- ▶ Environmentally aware: 96% of Generation Y want an environmentally aware workplace
- ▶ Flexibility: 56% of Generation Y prefer to work flexibly and choose when to work, and 79% prefer to be mobile rather than static workers

Generation Y already represents over a quarter of the world's population and the proportion is growing as shown in figure 5. Not only will the members of Generation Y be among the most powerful consumers in history; as they enter the workforce, their impact there will be equally impossible to ignore. Generation Y display the same lack of patience as employees as they show as consumers, and companies must address their evolving expectations to avoid high recruitment and churn costs. What is more, this generation have significant ideas and are willing to share them company-wide, they represent a useful resource every company should listen to.



The challenge

Facing the implications of digital change

Loss of control over the customer relationship

The proliferation of digital channels and devices gives consumers greater access to information, and the means for communication and collaboration. The physical world is being replicated in the digital world through digital communities, businesses and assets, fundamentally changing the way consumers engage with businesses and each other.

Information aggregation and price comparison have evolved. Consumers now have real-time, mobile access to data that they previously relied on brands to provide them with. Today's consumer has real-time access to competitive pricing information simply by scanning a product barcode into their mobile phone and reading this information through an application such as Red Laser. In this way price transparency is increasing as consumers can compare the prices of products on the move, placing power firmly in their hand.

As well as relying on brands for pricing information, consumers also used to rely on brand communication and brand values to make informed choices, but this is increasingly not the case. Today's consumers trust each other more than they trust corporations and/or brands (78% of consumers trust peer recommendations versus 14% who trust advertisements)⁵. They advise each other, and what's more, they heed each other's advice. Tripadvisor, the free online peer-to-peer travel review site has

over 45 million reviews and opinions and 6 million photos of travel destinations⁶. These millions of conversations between potential consumers that are happening around a brand can be a frightening concept for organisations used to controlling the brand message, however, the rise of the 'prosumer' is also an opportunity for brands to increase engagement. As well as advising each other, prosumers should be used as a source of vital product development ideas for brands, as Walkers crisps discovered with their 'Do us a flavour' campaign, a social media initiative that invited consumers to generate ideas for the next flavour of crisps. Microsoft recognises the benefit of this force of 'Most Valuable Professionals' who provide "real world answers" to solve product difficulties and provide feedback⁷.

Brands are facing a loss in the information monopoly and a shift towards two-way communication and conversation. It is vital that brands embrace the shift in consumer power and find ways to make it work for mutual advantage. This is because as customers gain more power to choose where and how they interact, they will begin to choose a smaller number of organisations with which to maintain primary relationships. This is likely to be collaborative organisations that reflect and engage with their values. Other organisations thereby risk becoming mere suppliers. Not all organisations can win the battle to retain the customer relationship - the digital world has thrown organisations into a strictly competitive game.

The Rise of the Prosumer

A Prosumer is a term used for a consumer who is unusually interested in products/services of a brand. Prosumers will dedicate their spare time to upload reviews and comments and respond to other reviews and comments about the product. Some prosumers will record YouTube videos to help other users with technical service issues of a particular product. These individuals can be very useful sources of product development ideas, or can be incentivised as a low cost provider of technical service to other consumers.

The need to engage digitally with suppliers and employees

While companies tend to be aware of the need to achieve collaborative and cross-channel engagement with their customers, they are less conscious that this need applies equally to suppliers and to employees. The rise of social media is breaking down barriers between these groups. Instead of talking one-on-one to customers, suppliers and employees, organisations are now talking to a crowd of people who are often talking to each other. As well as generating a great deal of noise, this interaction means that information can flow in directions that the company did not anticipate.

Generation Y, in particular, have had experiences as customers which influence their expectations in other business dealings, such as their interactions with their employers. That means that, as well as cost savings and productivity benefits, digital communication capabilities are becoming a key weapon in recruiting and retaining talent. Gone are the days when an employee enthusiastically received their new work laptop and

mobile phone. Today's employees more often than not have more information communications technology at their personal disposal than they are given at work, and IT departments are increasingly seen as a limitation to their needs rather than an enabler. Organisations must understand the best way to enhance communication capabilities for their employees. For most firms, this will not involve handing out tablets or iPads to each employee, but it should involve, at a minimum, setting up internal social networking and knowledge share sites.

The same need applies to suppliers and partners. The expectations that are being formed in the B2C world are transferring to the B2B world as well, and increasingly suppliers and partners will look for ways to engage digitally with each other. There is a need for greater focus on security in the B2B world, but the same advantages of collaboration and knowledge sharing are to be gained. Organisations should look to integrate eprocurement into their supplier relationships to reduce manual processes and improve invoice tracking, or develop secure portals for real-time collaborative forecasting with suppliers to better manage inventory.

Barcode reader app 'Red Laser' has had over nine million downloads since its launch in 2009, allowing users to scan barcodes and QR codes to check prices, create shopping lists and find reviews



Organisations are wondering, or perhaps fearing, what Google will do next



Increased competition and the risk of commoditisation

We have already identified the future trend of consumers choosing to invest their total acquisition with a smaller set of brands. This trend is emerging as a result of two forces coming together: Consumers want choice, without the cost of developing and maintaining multiple relationships; and companies are continually seeking ways to retain and develop increased share of wallet through deeper customer relationships. These two forces are made possible by digital advance and globalisation.

Digital channels lower barriers to entry and increase globalisation, leading to a spiral of intensifying competition and commoditisation. Innovative organisations are taking the opportunity to diversify, bringing cross-industry convergence and blurring of the boundaries between industries. Previously physically distinct products and sectors now compete with one another, over less clearly defined customer bases.

In this way, there is an extension of 'superbrands', such as Tesco, Google or Virgin. Already, supermarkets compete with insurance providers, energy companies offer credit cards and retailers offer energy discounts. Google, is today in direct competition with social networking sites, they have also moved into the mobile handset market, and even the online fashion market, leaving organisations in other industries wondering, or perhaps fearing, what Google will do next. The battle to 'own' the digital customer has been thrown wide open.

As a consequence, all industries are facing commoditisation, some sooner than others, as figure 6 shows. This threat arises because as more and more information becomes available to customers and competitors, and non-traditional players enter the market, prices, values and product characteristics all tend to converge. Price comparison, and unbundling of products, means that the margin play is becoming more and more transparent, and less and less acceptable to consumers.

To reduce the impact, many organisations are successfully shifting their focus from products to services as a way of differentiating themselves and also increasing margins. Companies should look to create new information asymmetries, which make it more difficult for customers to directly compare providers, and focus on innovation that can truly revolutionise and disrupt the market. Successful responses to the commoditisation threat include increased personalisation; wrapping a service around a product; and a re-bundling of products to realise price advantages. Nike allow customers to personalise large aspects of their product range through NikeiD; Apple and Amazon have successfully integrated their products with service propositions; and publishing houses such as Random House and BBC Books are partnering to create a set of re-bundled ebook and television series products.

It is through differentiation and innovation that organisations can create the shift in mindset necessary to win in the digital game.



What needs to happen

The need for an end-to-end response

Many companies are already developing responses to the challenge of digital by moving from a transactional to an 'interactional' relationship with their customers. They are inviting their customers to become part of the R&D process, the design process and the go-to-market. They are also encouraging them to participate in the post-sale support process, and taking advantage of 'prosumerism' as a low-cost way to provide service.

However, forward-looking companies need to do more than this. To succeed in the digital world requires embracing innovation and identifying new engagement models and new business models. It requires grasping new opportunities that exist outside traditional markets and looking for the tools that will differentiate between the mere suppliers and the 'lifestyle partners' of the digital age.

We believe that the digital revolution, and its consequences, offer a great opportunity to transform. However, capturing the rewards of a digital world requires considerable commitment and a proactive approach. It is not enough to have a social media strategy. Companies need to develop a comprehensive 'digital strategy' that reaches far beyond the marketing department to tackle issues like ubiquitous cross-channel connectivity, social commerce, and the threat of commoditisation. Creating and adopting a strategy of this kind requires strong senior leadership, a focus on the customer experience management, and innovation within the operating model.

The need for new business and operating models

There are important lessons to be learned from the internet revolution. Firms that have capitalised on its possibilities have re-written the rules of entire industries such as music and advertising, and internet-enabled business models such as cloud computing have experienced tremendous growth.

It is this transformation of business and operating models that is needed to stand the test of time in the digital era. This lesson is starkly illustrated in the high-street by the failure of many bricks and mortar business models to adapt to the threat of Amazon. To be successful now, we believe, requires no less than the creation of enhanced or new business models, new operating models, new ways of interacting with consumers, and new ways of selling.

Even the giants of technology are recognising the need to shift and adapt business models. In recent months, Google have launched social networking site Google+ to rival Facebook, and Microsoft have launched the cloud version of Microsoft Office in Office365 to stave off completion from GoogleDocs and similar applications. A commitment to innovation means that even giants need to be agile.

Organisations therefore need to develop end-to-end digital engagement strategies and comprehensive digital operating models that address suppliers and employees just as much as customers. They must decide whether they can enhance or transform their existing models, or whether they need to invent a new model.



Option	Description	Example	Benefits	Value
1. Use digital technology to enhance traditional business models	Use automated and digital services to compete with and extend existing manual services	<ul style="list-style-type: none"> ▶ eBay auction model ▶ Life insurance computing algorithms ▶ Dell/Amazon - dynamic pricing 	<ul style="list-style-type: none"> ▶ Make better use of self-service channels including customer service through social media 	<ul style="list-style-type: none"> ▶ Reduced cost to serve ▶ Reduced time to revenue
	Shift the core business model from selling products towards offering services	<ul style="list-style-type: none"> ▶ IBM ▶ Streetcar/Zipcar 	<ul style="list-style-type: none"> ▶ 'Pay as you go' model extension 	<ul style="list-style-type: none"> ▶ Increased share of value-chain and share of wallet
	Transform hardware offerings into service offerings	<ul style="list-style-type: none"> ▶ Xerox/HP offering 'Managed Print Services' ▶ Apple/Amazon integration of product with ongoing service (iTunes) 	<ul style="list-style-type: none"> ▶ Integrating products with services engenders combined loyalty ▶ Longer-term relationship with customer 	<ul style="list-style-type: none"> ▶ Increased annuity revenue streams from services ▶ Increased customer lifetime value
2. Transform existing business models digitally	Offer entirely new services that cannot be provided manually	<ul style="list-style-type: none"> ▶ Google/Yahoo - online search capability ▶ Skype - VoIP ▶ Salesforce.com - software-as-a-service ▶ Facebook/LinkedIn - social media marketplaces 	<ul style="list-style-type: none"> ▶ Volume of potential customers using the often free service 	<ul style="list-style-type: none"> ▶ Shareholder and reputational value
	Offer existing services through new digital channels	<ul style="list-style-type: none"> ▶ 100flowers - purchase through Facebook ▶ Tesco - purchase through smartphone app ▶ Dell - customer service through Twitter 	<ul style="list-style-type: none"> ▶ Customer convenience engenders loyalty 	<ul style="list-style-type: none"> ▶ Increased revenue streams ▶ Reduced cost to serve
3. Invent entirely new business models or different engagement models	Offer entirely new revenue generating products/services, or different engagement models	<ul style="list-style-type: none"> ▶ Virtual currency used in online games and social networks ▶ Google/Yahoo - Advertising revenue linked to search ▶ Facebook - sell digital customer data ▶ giffgaff - a 'people-powered' mobile operator business model 	<ul style="list-style-type: none"> ▶ First to market ▶ Fast to market through digital channels ▶ High customer loyalty and low cost to serve with giffgaff 	<ul style="list-style-type: none"> ▶ New revenue streams

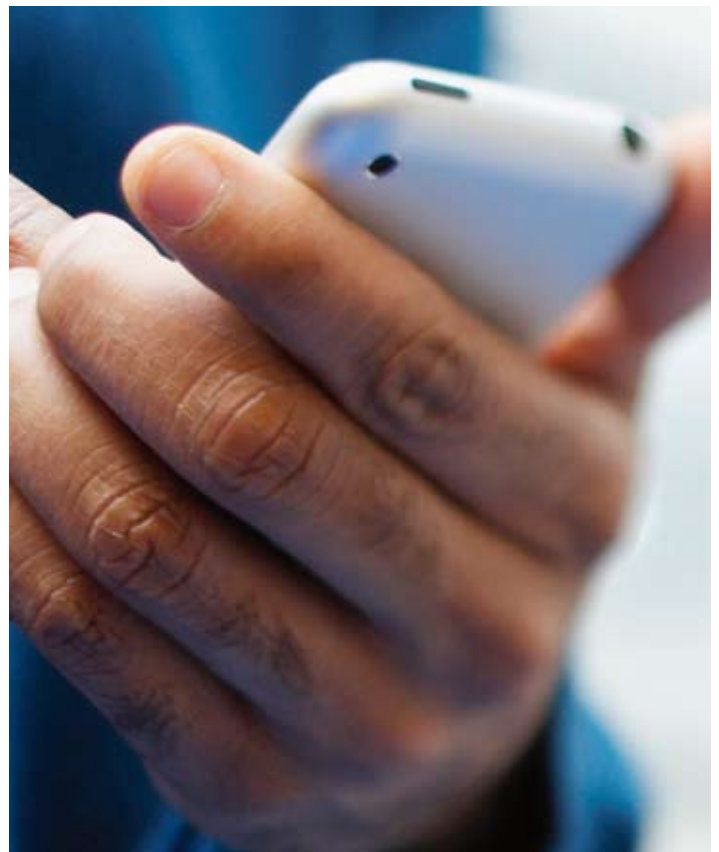


giffgaff

giffgaff is a Mobile Virtual Network Operator, buying airtime from parent company O2. It does not run any call centres: instead, members help each other answering questions in the company's forums, thereby reducing cost to serve. Nor is there any TV advertising: members spread the word to attract new customers, receiving financial incentives to do so.

This business model allows O2 to attract a different type of 'free-thinking' Generation Y customers who are disillusioned with the traditional mobile operating models. giffgaff customer satisfaction is rated at 90%. 31% of customers came from long-term mobile contracts with other providers. 63% of them recommend the service to friends or family members, and 78% of recipients of these recommendations become registered members.

Agility is important, but for some brands, the risk of adopting new and disruptive business models is that certain customers become uneasy with the change. In this instance, or even if organisations are looking to 'experiment' with digital business models, then an additional option is to spin off smaller businesses in order to learn how to take advantage of the new digital world. This is the strategy of giffgaff (see panel). This 'people-powered' mobile operator is owned by O2, but, as its creator confirms, is not in competition with O2, but is 'operating in a different space to meet the needs of free thinkers'⁸. This is not a new concept, the same successful strategy was adopted by HSBC when they launched FirstDirect under an independent brand name, to entice a new type of customer without rejecting their loyal followers. Succeeding in the digital world is not about 'out with the old and in with the new'; it is instead about truly understanding the needs of your customers, the shifts in your market place, the differentiation strategy of your business, and the best means for achieving success.



Conclusion

A new kind of consumer means new ways of doing business

Today, most companies are either thinking about or pressing ahead with digital transformation initiatives. Every company has a website, and few marketing strategies are signed off without incorporating social media. Certainly, social media is a critical component of any digital strategy, but a holistic response to the digital shift must go much further.

The digitisation of everything is a step change even greater than the invention and adoption of the internet, primarily because of its scale and pace of change. What we describe today as 'digital' in a few years time will have no need for the descriptive word. A 'digital camera' is already a mere 'camera' to those who know no different. In the same way, a 'digital' strategy will become business as usual strategy. This is why it is so important to get a head start and learn while there is still time.

Digital is changing the world, and progress is not linear. In a world where a smartphone is no longer just a smartphone, but a potential revolution⁸, we invite organisations to explore what digital advances mean for them and their stakeholders.

We support the opinion of executives who view digital much more as an opportunity to be tapped than as a risk to guard against. Not every digital initiative will work for every organisation, and it is important to assess capability and capacity for change before deploying a digital strategy. In general, though, the more holistic the initiative, the greater the chance of success. We believe that those who act holistically, and act now, stand to gain the greatest competitive advantage.

How is Ernst & Young positioned to help?

Please contact Richard Ingleton (ringleton@uk.ey.com), Yunus Ozler (yozler@uk.ey.com) or Pippa Thomas (pthomas@uk.ey.com) at Ernst & Young if you are interested in further exploring our digital offerings. We would be happy to assist your organisation in identifying digital opportunities across customers, suppliers, investors, leadership and employees.

Notes

1. <http://techliberation.com/2009/05/28/on-measuring-technology-diffusion-rates/>
2. Core Edges Blog, 'Core Digital Infrastructure Technologies improve exponentially without stabilising', 26 June 2009
3. Ericsson, 'Vision 2020, 50 Billion Connected Devices', February 2011
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5. www.tripadvisor.co.uk
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7. www.contagiousmagazine.com, 'Reinventing Mobile / An Interview with giffgaff's Gave Thompspon', 22 March 2010
8. Economist Intelligent Life, 'Digital Africa', March 2011



For more information about our views on Digital and to see more, please contact your local Ernst & Young office or visit www.ey.com



Digital data opportunities



Social media



Digital in utilities

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