

# **Surfcontrol**

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**A Case Study which uses the Strategy Compass**

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## **Introduction**

Surfcontrol PLC is one of the worlds leading developers of enterprise Web and email filtering software. Its software is used to monitor and manage Internet access, instant messaging, and e-mail communications. Currently Surfcontrol employs more than 500 people in 13 offices across the United States, Europe and Asia/Pacific.

The company's products and technology are used by more than 20,000 customers worldwide. Many corporations, government agencies, educational institutions, and to a lesser extent, home users use Surfcontrol's software. The organisation has built up strong partnerships with companies such as IBM, Cisco, Check Point, and Microsoft who resell products and services which integrate its content filtering technology.

This document will initially look at how the company has used innovation and entrepreneurship to become one of the leading players in the global content security market. It will then cover a strategic analysis of Surfcontrol using the Strategy Compass and, on the basis of this, outline steps recommended for steering this organisation to greater success.

### ***Surfcontrol: Innovation and Entrepreneurship***

When thinking about monitoring and managing Internet/email usage many would initially think of restricting access to pornography and reducing SPAM emails. Indeed these are the areas the fledgling Surfcontrol (or JSB software technologies PLC as it was then known) focused on when it began developing software back in 1996. Its products gained a reputation for being extremely effective in blocking these threats and indeed any employee looking at porn now would be extremely foolish indeed.

### **Process needs**

In the early days of managing Internet usage companies relied on a mix "stopwatch" technology and blacklisting to limit Internet usage by their employees and restrict access to pornography related sites. Surfcontrol continued to build on its strengths in these areas but, by analysing Internet usage trends in the workplace, it realised that as the scope of the Internet grew it could not continue to base its products on such simplistic rules.

A report carried out by IDC in August 2004 reported that "30-40% of Internet use in the workplace is not related to business". Surfcontrol realised this at an early stage but who is to say what determines Internet usage related to business? An employee working in a bank who is looking at a lingerie site may be frowned upon but would this be the case for someone working for Victoria's Secret? To resolve issues like this Surfcontrol incorporated means of defining areas of interest so companies could define what they determined as appropriate and inappropriate. This could be tailored for work functions in an enterprise or even down to individual users.

Drucker describes this area of opportunity within an industry as “process needs” one of four “sources of innovation”. For the entrepreneur, opportunity is based on innovation. As Peter Drucker points out, “Innovation is the specific function of entrepreneurship ... It is the means by which the entrepreneur either creates new wealth-producing resources or endows existing resources with enhanced potential for creating wealth” (Drucker, 1985). Surfcontrol is indeed enhancing its offering and therefore enhancing its potential for creating wealth through increased sales.

## **Quality**

*“Firms with the highest relative quality ought to have the highest returns.”  
(McNamee 2004, p.74)*

Internet related technologies (and associated threats caused by malicious technologies) change at a phenomenal rate so something which is seen as being cutting edge today may be superseded by even more advanced technology in 6-12 months time. It could be argued that the timescale used by PIMS for measuring the “Degree of Innovation” described as “The percentage of a firm's revenues that come from products introduced in the last 3 years.” (1973 cited McNamee 2004, p. 54) may skew ones view of how this might impact Surfcontrol's profitability.

Surfcontrol continually has to innovate so that not only is its service offering improving constantly to meet these new threats but also that its relative quality is maintained in relation to its competitors. Recent figures show that, not only is the company maintaining its relative quality lead and strong market share, it is also increasing its' profitability and ROCE. This confirms McNamee's' (2004, p. 54) view that “for today's pioneering firms: if a pioneering firm wishes to retain its market leadership then achieving superior quality, right from the start, is essential.”

## Surfcontrol's recent performance

Surfcontrol's performance over the years 2003 to 2004 has been taken from its 2003 and 2004 annual reports and it is presented below in the Strategy Compass format. Additional information was taken from the FAME (Financial Analysis Made Easy) database published by Bureau van Dijk Electronic Publishing.

**Table 1: Strategic position of Surfcontrol PLC<sup>1</sup>**

Surfcontrol PLC	2003	2004	% Change	Comments
<b>Competitive Position</b>				
Sales (£k)	44367	47952	8%	Positive
Mkt Sh(%)	13	11	-15%	Negative
Mkt Sh of Largest Rival	12	13	8%	Negative
RMS (%)	1.08	0.85	-21%	Negative
Relative Quality H, E, L	High	High	N/A	Positive
Price Rel to Competition H, E, L	Equal	Equal	N/A	Positive
New Products/ Sales (%)	50	40	-20%	Positive
R&D expend/ Sales (%)	10.28	11.14	8%	Positive
Marketing expend/ Sales (%)	14.88	13.81	-7%	Positive
<b>Asset utilisation</b>				
Investment (£k)	20358	25807	27%	Negative
Plant and Equipment at Cost (£k)	1997	9142	358%	Negative
Sales /Total Assets (£k)	1.98	1.71	-14%	Negative
Number of Employees	428	464	8%	Negative
Sales /Employees (£k)	103.66	103.34	0%	Neutral
Capacity Utilisation (%)	80	85	6%	Positive
<b>Leadership and Behaviour</b>				
Leadership (G, A, P)	Good	Good	N/A	Positive
Labour turnover	Low	Low	Low	Positive
<b>Markets Addresses</b>				
Market size (£k)	341285	447083	31%	Positive
Demand (% Volume growth)	27	31	15%	Positive
Life cycle	Growth	Growth	Growth	Positive
No. of Immediate Customers accounting for 50% of Sales	114	80	-30%	Positive
% of Demand Controlled by 4 largest Companies	40	42	5%	Positive
Typical Purchase Amount	£2,218.00	£2,398.00	8%	Positive
<b>Profitability</b>				
Net Profit (£k)	3855	6335	64%	Positive
ROCE (%)	17.24	22.58	31%	Positive

<sup>1</sup> Assumptions and notes supporting the Strategy Compass table can be found in the appendix at the rear of this document.

## **The Strategy Compass analysis of Surfcontrol PLC**

Now, an analysis of Surfcontrol's strategic position will be carried out using the Strategy compass.

### ***Competitive position***

Surfcontrol has a strong competitive position. While its PIMS RMS has slipped from 1.08 to 0.85 over the course of the 2 years analysed it could be argued that this has more to do with the company expanding into new markets rather than losing share in its original markets. This expansion has included adding new products as well as new features to existing products which bring it into direct competition with competitors in other markets outside its core Internet security one

It is positive to see relative quality maintained while also maintaining an equal relative price. Innovation has been brought down to a more manageable 40%. This should put the company in a great position to build on an already strong competitive position and help it compete with new competitors in the markets it is moving into.

#### **Competitive position strategy: -**

- Try to regain market lead; with a continued high relative quality aim for small price increases to increase sales
- A further increase in marketing spend can be afforded to drive home to customers relative quality strengths

### ***Asset utilisation***

Asset utilisation appears to be the main problem area for Surfcontrol at the moment. Increases in investment and plant and equipment costs have had a negative impact on asset utilisation. With sales dropping from £1980 to £1710 for every £1 of assets this drop must be addressed immediately to prevent it having a major impact on the profitability of the business. Though the company seems to have managed to negate this issue elsewhere with an increasing ROCE figure, I would urge against complacency. The market may not always be so favourable with growth figures up around 30%.

#### **Asset utilisation strategy: -**

- Reduce investment intensity as a matter of urgency though asset reduction and increasing sales
- Sales per employee needs to be improved by perhaps introducing incentives or improving existing ones

## ***Leadership***

Leadership within the organisation appears to be very good with the company receiving a number of awards for strategic leadership as well as for product quality over the last two years.

### **Leadership strategy: -**

- Try avoiding any major disruption to senior management line-up.
- Keep labour turnover low; reward staff for innovative new ideas to keep product line-up cutting edge and fresh

## ***Markets addressed***

Surfcontrol is in the enviable position of operating in a market which is forecast to grow at around 31% for the next 4 years. It is making strategic alliances with the major players in the IT industry. Not only is this increasing its access to markets but it is also helping to share the costs associated with selling its products. This can be seen in the reducing number of customers accounting for 50% of sales.

### **Market strategy: -**

- Reduce number of customers further; focus on large resellers not individual buyers
- Increase customer purchase amount

## ***Conclusions***

Overall Surfcontrol appears to be in a very strong competitive position in a rapidly expanding market. Its leadership appears to be very adept in plotting a strategic course through what is a rapidly changing business environment. One black spot on its strategy compass is its investment intensity but if the strategies outlined above are followed this should be addressed successfully.

### **Firm perspective: -**

- **Core strategy:** Reduce investment intensity, increase customer purchase amount
- **Strategic agenda:** Asset reduction to remedy investment intensity. Increase ticket prices to take advantage of higher relative quality than competitors.
- **Profitability:** Increasing ticket price and reducing investment intensity should maintain growth in ROCE

## References

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## Appendix

### ***Assumptions and notes supporting the Strategy Compass table***

While a large amount of data contained in the Strategy Compass table was readily available from Surfcontrol's annual reports and the FAME database a number of assumptions have been made based on data available in the public domain.

1. Market share for Surfcontrol and that of its largest rival (Websense) for the year 2004 was assumed based on the sales and market growth figures outlined in the 2004 annual reports of both companies
2. Relative quality and Price relative to competition is based on personal experience of purchasing and using Surfcontrol products as well as experience of work colleagues.
3. New product sales have been assumed to have reduced between 2003 and 2004 due to a reduction in the rate of new product releases over the period from 2000 to 2001.
4. While marketing spend versus sales has went down, actual marketing spend was noted in the 2004 report as having increased. While no actual figures were given, a 10% increase in marketing spend was assumed due to total cost of sales having also grown by 10%.
5. A high capacity utilisation was assumed due to the nature of Surfcontrol being an Internet driven business. Customers can avail of the latest information regarding the company's products 24/7 from their website as well as take part in on-line product demo's and training sessions offered by various Surfcontrol sales offices in different time zones. Customers are also able to download trial and full versions of software online any time of the day or night.
6. Leadership is assumed to be good due to the growth in revenues year on year from 1998 onwards, increasing net profits; increasing ROCE plus low labour turnover showing a labour force that have faith in their leaders. Surfcontrol was also the recipient of the Frost & Sullivan Award for Product Line Strategy Leadership 2004.
7. Labour has grown organically as shown by figures taken from the annual reports. Labour turnover is assumed to be low.
8. Market size is assumed given market growth figures given in the annual reports. These growth figures themselves are taken from reports on the Global Content Security Market (Source: IDC, 2003)
9. No. of Immediate Customers accounting for 50% of Sales for 2004 is assumed based on Surfcontrol's reported 2003 figures as well as reporting in 2004 that indirect sales i.e. Sales through value added resellers and channel partners had increased.