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Microsoft: A Strategic Audit

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Abstract

This thesis is submitted in partial fulfillment of the University Honors Program Requirements. It discusses Microsoft Corporation and its placement within the tech industry using different analyses such as PEST, Porter’s, and SWOT. In addition to its placement, the thesis explores what strategies Microsoft could pursue next. The industry is highly competitive, so Microsoft needs to stay on its toes and continue to build upon its strengths to remain at its current competitive level. The cloud industry is rapidly growing, so it would be best if Microsoft used its global presence and existing infrastructure to build upon its existing cloud platform and expand it as much as possible.

Keywords: strategy, strength, weakness, opportunity, threat, competitive, technology, cloud
Background and Issues

Company Background

A hobby between two friends, Bill Gates and Paul Allen, of writing and testing computer programs became the driving force behind the creation of one of the world’s largest technology companies, Microsoft Corporation. Microsoft began dominating the software industry in the mid-1980s with MS-DOS. Now, Microsoft dominates in the tech industry with a current market cap of over 900 billion dollars by developing, manufacturing, licensing, supporting, and selling computer software, consumer electronics, personal computers, and other related services (“Microsoft Corporation - Company profile…”).

Company History

Born in 1955, Bill Gates and Paul Allen started writing computer programs for fun and profit at the age of 14. In 1975, after writing a version of BASIC for the new Altair microcomputer, Gates and Allen founded Microsoft and relocated to Albuquerque, New Mexico. After creating multiple programming languages, such as FORTRAN and COBOL, Microsoft became the leading distributor of microcomputer languages (“Microsoft Corporation - Company profile…”). By the end of 1978, Microsoft had 13 employees and one million dollars in revenue. On June 25, 1981, Microsoft became a corporation. Today, Microsoft is based in Redmond, Washington, and has over 130,000 employees worldwide with the mission “to empower every person and every organization on the planet to achieve more” (“Facts about Microsoft”).

Situation Analysis

Business Model

As said in Microsoft’s 2018 annual report:
“Founded in 1975, we develop and support software, services, and solutions that deliver new value for customers and help people and businesses realize their full potential. Our products include operating systems; cross-device productivity applications; server applications; business solution applications; desktop and server management tools; software development tools; and video games. We also design, manufacture, and sell devices, including PCs, tablets, gaming and entertainment consoles, other intelligent devices, and related accessories. We offer an array of services, including cloud-based solutions that provide customers with software, services, platforms, and content, and we provide solution support and consulting services. We also deliver relevant online advertising to a global audience,” (“Annual Report 2018”).

Following Satya Nadella’s transition into CEO, Microsoft has become increasingly more focused on artificial intelligence, cloud services, mixed reality, and quantum computing. However, only a third of their revenue comes from cloud services. The other two-thirds are from commercial and personal computing.

**External Analysis**

Microsoft’s main competitors are Amazon, Apple, Facebook, and Google (“Annual Report 2018”). Amazon rules the cloud services market with 32.3 percent market share at the end of 2018, while Microsoft has 16.5 percent and Google has 9.5 percent. Microsoft’s growth was higher in 2018 than Amazon’s, but less than Google’s, so the competition is coming from both sides. Microsoft’s search business competes with Google and a wide array of websites, social platforms like Facebook, and portals that provide content and online offerings to end users. Communication services from Microsoft such as Skype, Skype for Business, and Teams all
compete with Google and Facebook who also have a variety of messaging, video, and voice communication providers.

Apple and Google have various software products including their respective operating systems and alternative platforms and devices, such as the MacBook and Chromebook, that directly compete with Microsoft and its operating system, Windows, as well as its personal computers. Further, Apple and Google distribute versions of their pre-installed application software, such as mail or calendar products, through their PCs, phones, and tablets, which compete with Microsoft’s computer applications.

Microsoft’s gaming platform competes with console platforms from Nintendo and Sony, both of which have a large, established base of customers. Microsoft’s video game competitors include Electronic Arts and Activision Blizzard. Xbox Live faces competition from various online marketplaces, including those operated by Amazon, Apple, and Google.

An analysis of Porter’s five forces should further explain the industry that Microsoft is in.

1. Competitive Rivalry (Strong):

Across Microsoft’s various markets, there are a plethora of competitors. With tech powerhouses such as Google, Amazon, Apple, Facebook, and Microsoft all in the same bowl, everyone needs to stay on their toes. Some products are easier to switch between than others, but, for the most part, the cost of switching isn’t too high, so companies must continuously put in effort to keep their grasp on customers (“Microsoft Corporation’s five forces analysis…”).

2. Bargaining Power of Buyers (Moderate):

It isn’t unlikely for customers to opt out of a company’s services if different services provide better value. For instance, if customers need a cloud services platform with more
enterprise experience, they may take Microsoft over Google. However, if customers need a cloud services platform with industry-leading tools in artificial intelligence or data analytics, they would likely prefer Google ("AWS vs. Azure vs. Google: Cloud comparison [2019 update]"). Also, information about the industry’s products and services is easily accessible online, so it’s quite easy for buyers to compare competitors and see which would provide them with the best value ("Microsoft Corporation’s five forces analysis…").

3. Bargaining Power of Suppliers (Low):

Depending on the company, suppliers hold low to moderate power in this industry. Microsoft’s line of personal computers and gaming consoles may require specific materials, which some could say gives the supplier a bit more power. However, Microsoft and many of its competitors are such large forces that suppliers wouldn’t want to risk losing them as customers. Pegatron manufactures Microsoft’s Surface line of personal computers, but it has an overdependence on the computing sector for revenue ("Pegatron SWOT analysis, competitors & USP"). Thus, Pegatron wouldn’t make any moves to jeopardize its relationship with Microsoft when the cost of switching suppliers is low ("Porter’s 5 forces"). Samsung, on the other hand, may have a bit more power over some of its customers than Pegatron does over Microsoft because of its dominance in the OLED display market ("Samsung has 93% of the smartphone OLED display market").

4. Threat of Substitutes (Low):

In respect to the industry, the threat of substitutes is low. For the force to be high, substitutes would need to offer something uniquely different and provide tremendous value compared to the current products and services in the industry ("Porter’s 5 forces").
However, it’s rare for such substitutes to exist when technology is already incredibly advanced. In respect to Microsoft, the threat of substitutes can vary depending on the market. When it comes to the operating system market, the threat of substitutes for Microsoft’s Windows is low. Although Apple and Google have their own operating systems, the switching cost for customers is too high to justify. Although, when it comes to the gaming market, threat of substitutes can be moderate for Microsoft. Depending on the customer, Microsoft could lose users to Sony for their line of highly ranked, exclusive video games, or even Google to their new Stadia cloud gaming platform.

5. Threat of New Entrants (Moderate):

It isn’t too difficult to enter the industry, but it’s very difficult for new entrants to gain the same brand recognition and userbase that tech giants have. Although many operating systems have been created, most don’t have the users or previous knowledge like Apple or Microsoft to make a dent in the operating systems market, so threat of new entrants is low in that regard (“Microsoft Corporation’s five forces analysis…”). Previously, I would’ve said the same for the gaming market because the major players have always been Microsoft, Sony, and Nintendo, but with Google’s announcement of Stadia and its pivotal cloud gaming technology, I’d say Google is a moderate threat. For the most part, the threat of new entrants is low for Microsoft across its various markets because of its brand, users, and enterprise experience.

To better understand the macro environment of Microsoft, let’s analyze it using PEST.

1. Political:

The technology industry has been facing a lot of hurdles lately. Over the years, Microsoft has received several fines by the EU for abusing its market dominance or
charging unreasonable royalty fees ("Here are some of the largest fines dished out by the EU"). After the EU’s General Data Protection Regulation (GDPR) came into effect recently, tech giants like Google and Facebook have been receiving enormous fines for alleged infractions. Increasing distrust in the tech giants, due to data leaks and privacy concerns, will likely urge lawmakers to create new federal privacy regulation separate from the GDPR.

2. Economic:

   The economy is doing very well right now and the technology industry is part of the reason. Technology plays a role in almost all major sectors of our economy – healthcare, transportation, education, manufacturing, energy – and demand for workers is growing rapidly ("The 5 industries driving the US economy"). With a growing interest in cloud computing, artificial intelligence, mixed reality, and machine learning, companies like Microsoft and Google are only going to profit. As said by Todd Thibodeauz, CompTIA president and CEO, “Technology is the generator that powers innovation, growth and breakthroughs in virtually every other sector of the economy; from advanced manufacturing techniques and innovations in transportation, to smarter, more livable communities, to advances in education, energy and healthcare.”

3. Social/Demographic/Physical Environment:

   Antitrust, privacy, and culture concerns have been on the rise. Tying into the Political issues mentioned before, it’s easy to see why people are hesitant to share personal data when data breaches and disobedience of data regulation happens so frequently. On top of that, the culture of the tech industry – particularly within
Facebook, Google, and Microsoft – has been under some heat lately due to the harassment of women within the workforce. As the tech industry’s image degrades, so will the images of those within the industry.

4. Technology:

Due to the insane amount of competitive rivalry within the tech industry, all companies need to keep up-to-date on current technology trends and on the technology their competitors create. They may even need to analyze the life cycles of certain technology to determine when the next big shift might happen (i.e., flip phone to smartphone). With how fast technology advances, this is quite difficult. For example, some say the cloud is the future of technology. With Amazon entering the cloud services market first, Microsoft and Google have some catching up to do.

As a conclusion to the external analysis of Microsoft, it’s worth looking at its opportunities and threats. Microsoft’s major threats include the other tech giants, lawsuits and regulations surrounding the tech industry and monopolies, and the general changing in the technology market and consumer preferences. However, Microsoft also has a plethora of opportunities within many markets, including, but not limited to, the commercial cloud market, the smartphone market with a new line of Surface phones, and the gaming market with a cloud gaming console that takes advantage of Microsoft’s incredibly large data network.

**Internal Analysis**

Although Azure is slightly behind Amazon Web Services in market share, Microsoft is still in strong standing in global marketplace in cloud segment. Microsoft offers a wide range of cloud-based computing services that include Microsoft Office 365, Skype, Azure, Xbox Live, and OneDrive (“Microsoft SWOT analysis”). In 2018 alone, Microsoft expanded its commercial
cloud gross margin to 57 percent, up 7 points year-over-year. As said in Microsoft’s 2018 annual report, “Azure’s competitive advantage includes enabling a hybrid cloud, allowing deployment of existing data centers with our public cloud into a single, cohesive infrastructure, and the ability to run at a scale that meets the needs of businesses of all sizes and complexities” (“Annual Report 2018”). All of this is thanks to Microsoft’s new CEO, Satya Nadella.

Since Satya Nadella took over for Steve Ballmer in 2014, he has effectively reinvented the company and made it more profitable than ever. Through leadership principles based on the values of learning, innovation, and creating a positive impact, Nadella has set Microsoft apart from competition in positive terms (“Microsoft SWOT analysis”). Being a global brand that is operational across more than 190 countries, Microsoft is used by millions international. In 2018, the company made $110.4 billion in revenue, $35.1 billion in operating income, and return $21.5 billion to shareholders through share repurchases and dividends (“Annual Report 2018”). Although it was only temporary, Microsoft even ended 2018 as the most valuable public U.S. company by market cap (“Microsoft closes out 2018 as the top public company”).

Microsoft’s weaknesses lie in its slow innovation, imitability of some products, and dependence on software. It has attempted to enter other markets that have been growing – smartphones, search, browsers, and advertising – but Microsoft’s innovation is slow compared to Google, Amazon, and Apple, which is a large reason why it can’t capture much market share in those separate markets. Microsoft’s innovation is less of a problem now with Satya Nadella as the CEO, but it has some catching up to do. Microsoft even tries to imitate some products, which has the possibility of reducing the strength of its brand. Moreover, Microsoft is extremely dependent on its software products, which weakens its business against competitors with dominant hardware and software products (“Microsoft Corporation’s five forces analysis”).
Microsoft uses broad differentiation as its competitive advantage, which can be seen in its mission “to empower every person and every organization on the planet to achieve more.” In other words, Microsoft has unique products that are sold to a wide variety of customers. These products are unique in their features, such as software designed specifically for business organizations. Also, part of Microsoft’s broad differentiation means that it sells its products to various market segments. For example, organizations, households, and individuals buy Microsoft’s products. Through broad differentiation, Microsoft attracts a large population of customers globally, building its competitive advantage (“Microsoft Corporation’s generic & intensive growth strategies”).

In summary, Microsoft’s main strengths lie in its extensive cloud segment, effective leadership, and high profitability and value through its global presence and brand recognition. However, Microsoft is slow at innovation and tries to imitate some products, causing its brand to take a hit. Based on Microsoft’s strengths and weaknesses, it needs to intensify its hardware development and improve product features to stay at a competitive level with the other large tech companies.

**Leadership Structure**

Microsoft employees feel quite satisfied with Satya Nadella as their CEO. After all, Nadella is ranked 20th as best CEOs of 2018 on Glassdoor based on employee reviews. A former employee said, “the direction and vision for the company are strong and I fully believe in CEO Satya Nadella’s direction for the company He’s made great improvements in the top leader ranks on culture change.” However, that same employee later says, “the new vision/direction and improvements are not consistent in all divisions/functions… Middle management does not align to the company values the top leaders are driving” (“Microsoft employee reviews”). After
looking at other reviews, it seems other employees – both current and former – have some of the same thoughts. Thus, Microsoft should have its top leaders review its middle management and put more control or policies in place so that they’re all on the same page.

**Strategy Goals**

**Goals and Objectives**

Microsoft should continue building upon its strengths to keep it as one of the most profitable companies in the world. While focusing mainly on its strengths, Microsoft should also dip its toes in areas it’s weak in, such as hardware.

**Evaluation Criteria**

To best evaluate different strategies, it’s helpful to use the SAF model. Thus, we’ll look at their sustainability, acceptability, and feasibility (“Evaluating strategic options using SAF strategy model”).

- **Sustainability:** Does it use the company’s strengths effectively? Does it overcome the difficulties identified in the analysis? Does it match the goals of the company?

- **Acceptability:** Does it benefit the stakeholders? Does it have an acceptable return rate? Is the risk worth it?

- **Feasibility:** Does the company have the resources, aptitude, and abilities to implement it and succeed?

**Strategy Alternatives**

**Build Its Commercial Cloud Platform**

As a rapidly growing trend in technology, the cloud is currently disrupting the IT industry. To keep up with its acceleration, Microsoft needs to continue to put resources into its cloud platform and services.
1. **Sustainability:**

   The cloud is all about connecting devices and making them more accessible to everyone, so it matches greatly with Microsoft’s mission. With an already strong cloud platform with Azure, Microsoft Office, and Windows, Microsoft can easily build upon its current strengths.

2. **Acceptability:**

   In 2018, Microsoft’s commercial cloud revenue increased by 56 percent to a total of $23.2 billion (“Annual Report 2018”). If Microsoft continues to make strides in the cloud, the risk will be low compared to the high return – as seen by its revenue growth since Satya took over as CEO and placed an emphasis on the cloud.

3. **Feasibility:**

   With an already incredible infrastructure and many data centers in place, it won’t be difficult for Microsoft to expand its cloud services. As a profitable company, and with the amazing increased in cloud revenue, Microsoft also has the resources to expand its infrastructure and data centers to strengthen its core.

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**Reenter the Smartphone Market**

Microsoft attempted to enter the smartphone market many years ago, but ultimately canceled its smartphone development efforts in late-2017 (“Departing Windows chief Terry Myerson explains why Microsoft failed in smartphones”). Built on a platform that wasn’t ready to compete with the abilities of Apple and Android phones, the Windows phone failed. However, Microsoft could learn from its mistakes and try to reenter with a new line of Surface phones.

1. **Sustainability:**
With a new line of Surface phones, Microsoft would be able to stick with its mission statement by giving people the ability to unify their Windows devices. With a Surface phone, people would be able to stay connected between their computers, phone, game console, and whatever other Microsoft devices they may have, empowering them to achieve more.

2. Acceptability:

Apple and Android devices dominate the smartphone market, so it would prove risky to enter. It would also be tough to sell the idea to investors, given Microsoft’s past attempt. However, as 5G comes closer to becoming a reality, and companies are experimenting with different phone designs (i.e., foldable phones), now may be the right time to try to enter again.

3. Feasibility:

Microsoft has a lot of resources, including an internal organization based around device and interaction. Surface devices have proven successful, so Microsoft could build upon that success and create a better base for the Surface phone. With an enormous amount of cash, it wouldn’t be difficult to fund, either.

Create a Cloud-Gaming Platform

The cloud is largely accepted as the future of gaming. With a dominant position in the gaming industry, Microsoft should create a cloud-gaming platform to build upon its current userbase and get ahead before Sony, Nintendo, or some other tech giant like Google takes away the opportunity.

1. Sustainability:
Creating a cloud platform for gaming would build upon Microsoft’s strong infrastructure and data centers, while taking advantage of its large base of Xbox Live users. Cloud gaming isn’t quite developed, so Microsoft could work on its weakness in innovation by releasing a unique, possibly pivotal product in the gaming industry.

2. Acceptability:

With cloud gaming still in its development stages, the risk is a little high. Gamers like their physical consoles, and a strong internet connection will likely be needed for cloud gaming, so it’ll be hard to sell such a new product. Although, some believe cloud gaming is the next revolution in gaming, so it could prove to be quite profitable.

3. Feasibility:

Microsoft is already a dominant piece in both the gaming industry and commercial cloud market, so it already has the resources to combine the two. However, with Google announcing its cloud-gaming platform, Stadia, Microsoft would need to dedicate a lot of resources to succeed as a competitor.

Strategy Recommendation

Continuing to build its cloud platform is the best strategy for Microsoft. It has the least amount of risk with the most reward, and Microsoft can take advantage of both the rapidly growing cloud market and its own infrastructure to succeed.

Strategy Justification

The cloud market grew 48 percent in 2018, which Synergy’s chief analyst, John Dinsdale, says is unusual for an industry of such scale ("AWS still king in public cloud, while Azure grows fast, IBM falls"). Although, it isn’t that surprising given Amazon’s, Microsoft’s, and Google’s
successful ventures in the cloud. Microsoft had its commercial cloud revenue increase by 56 percent in 2018 for a total of $23.2 billion ("Annual Report 2018"). Azure, alone, had its revenue increased by 91 percent, year-over-year, with analysts estimating it garnered $4 billion in the fourth quarter of 2018 ("AWS still king in public cloud, while Azure grows fast, IBM falls").

With such success is the still-growing cloud market, Microsoft would likely profit by putting more resources towards its cloud platform. Microsoft’s cloud platform is growing rapidly enough that it may be able to surpass Amazon in overall market share, too, which is an opportunity worth pursuing. Lastly, with significant research and development in quantum computing, Microsoft could ultimately lead a cloud platform that trumps the rest in speed and efficiency.

**Implementation Plan**

**Levels of Strategy**

- **Enterprise Strategy:** Create an intelligent cloud platform with comprehensive compliance coverage, unbreakable security, efficient tools, and fast services to meet evolving needs in the industry.

- **Inter-O rganizational Strategy:** Compete with Amazon Web Services and Google Cloud in the cloud platform business.

- **Corporate Strategy:** Put more resources into its cloud platform to take advantage of the cloud market’s current growth.

- **Business Unit Strategy:** Sell the cloud platform on its extensive usability, low costs per unit, data center coverage, and AI-based security. Microsoft is one of the two largest providers of cloud computing at scale, which is a very good selling point.
• Functional/Operational Strategy: Microsoft should sell its cloud platform as a globally used resource with significant computing power and trustworthy security, while the software and hardware should be upgraded to meet or exceed those standards.

Resources (Capital and Human)

At the end of 2018, Microsoft had $127.66 billion in cash and short-term investments (“Microsoft Cash and Short Term Investments (Quarterly)”). Taking a small amount of its cash would help tremendously with the research, development, and expansion of its cloud platform, likely returning its cost soon in the future. The current infrastructure and data centers Microsoft have in place for its cloud platform is on a global scale. However, if it wants to expand and surpass Amazon in market share, Microsoft will need to continually invest in more data centers and other infrastructure to support new and expanding services, especially if quantum computing is going to play a role down the line.

Contingency Plan (Trigger Point)

The cloud isn’t going to vanish into thin air, and Microsoft already has a good position in the market, so a good way to define the failure of this strategy is Microsoft’s progress in the market itself. If Microsoft not only fails at passing Amazon in market share but ended up decreasing its own so much that Google takes second, that would be the time to rethink this strategy. In the past, Microsoft’s Internet Explorer used to be the dominant web browser. However, after ignoring the development and improvement of the browser, Internet Explorer became obsolete to Chrome, Firefox, and many other browsers. Microsoft should know better than to do that again with the cloud market. After looking at competitors and what they all offer, Microsoft would need to rethink its placement within the market and try again. With resources already in place and the cloud here to stay, it’d be a waste to call it quits after one attempt.
Conclusion

Started by two computer programming enthusiasts, Microsoft Corporation has grown to be one of the largest and most profitable tech companies in the world. Although Microsoft had some rough times in the past with cultural issues, regulatory fines, and failed products, its new CEO, Satya Nadella, has boldly restructured and rebuilt the company, which can be seen today through Microsoft’s tremendous year-over-year growth. It was proven that jumping into the smartphone market was a risky move, so Microsoft should continue doing what it does best, which is build upon its current strengths and reap in the benefits, while slowly improving its weaknesses. If it does this, Microsoft will continue to be successful.


Hasleton, T. (2018). Departing Windows chief Terry Myerson explains why Microsoft failed in
