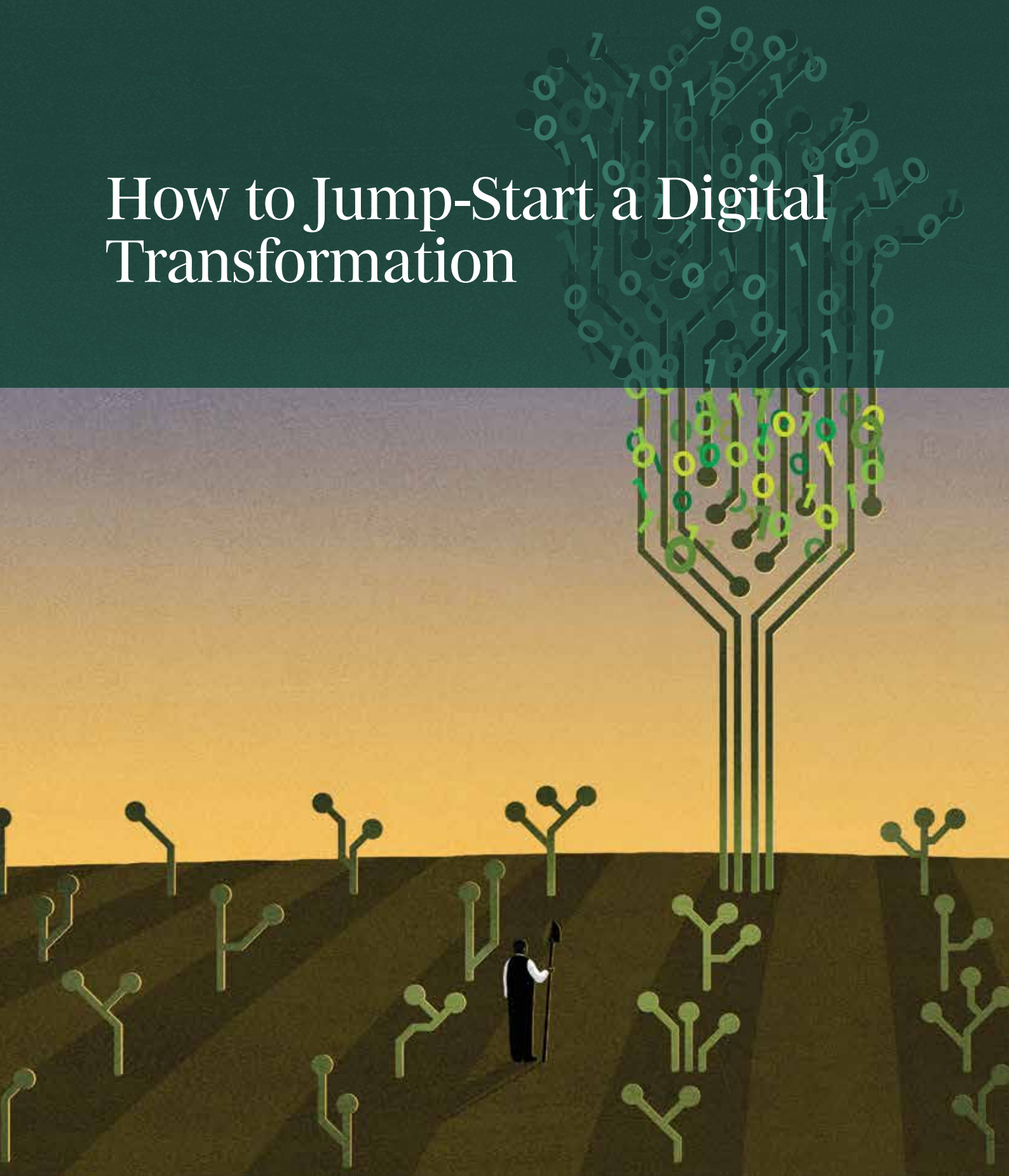


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# How to Jump-Start a Digital Transformation



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# How to Jump-Start a Digital Transformation

**Lars Fæste, Thomas Gumsheimer, and Matthias Scherer**

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## AT A GLANCE

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In industries such as energy, health care, industrial goods, and logistics, many companies have held off implementing digital technology because they lack the organizational mind-set and capabilities required to succeed. These late adopters need to embrace the concept of “fail fast and fail cheap,” developing their experience and digital capabilities through a three-step transformation framework.

### **SECURE QUICK WINS AT THE OUTSET**

Speed is more important than perfection. Companies should launch small-scale digital initiatives to improve the customer experience, bring new products and services to the market, and digitize internal processes.

### **SCALE UP SUCCESSFUL INITIATIVES**

Once they have identified promising digital ventures, companies need to scale them up and establish the right organizational model to integrate them with existing operations.

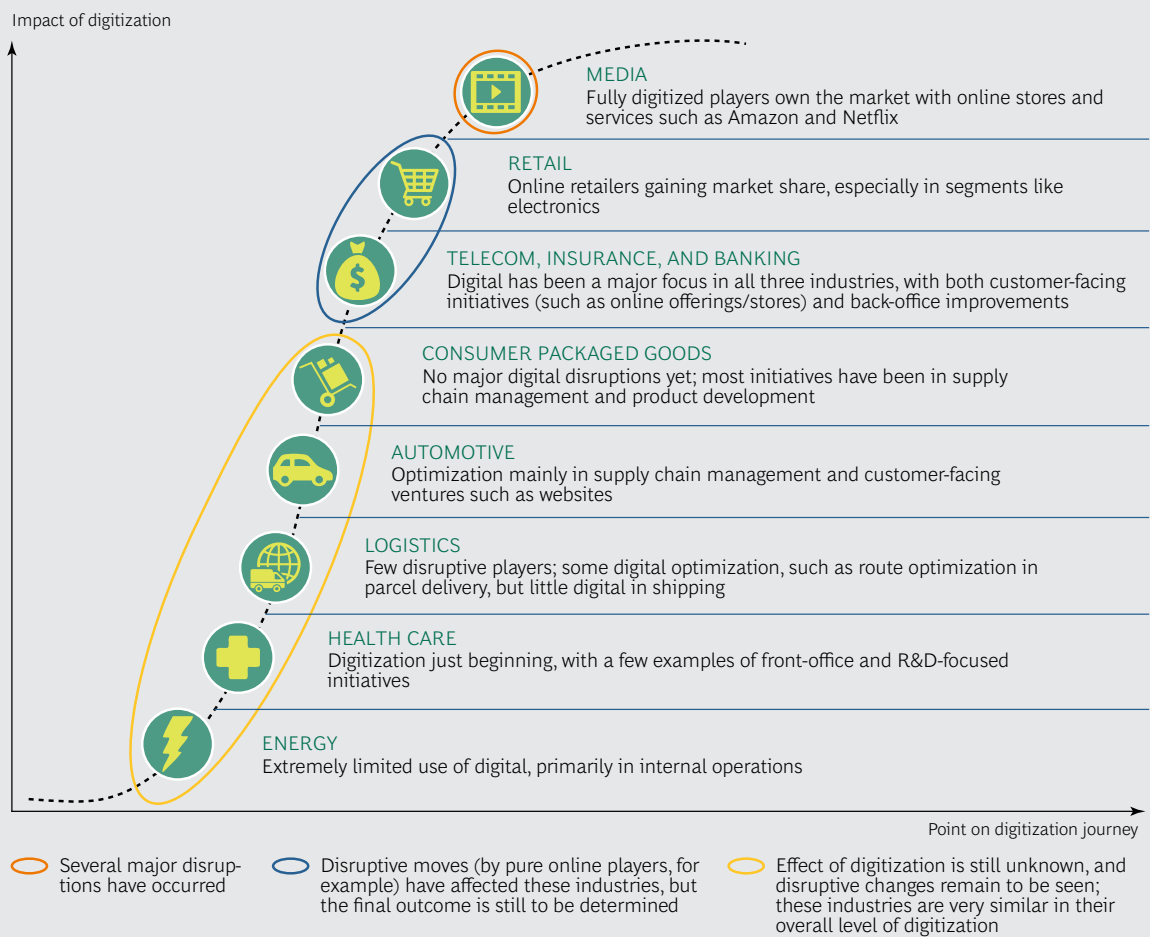
### **LEAD AND SUSTAIN CHANGE**

Successful digital transformations require strong leadership, alignment between IT and the business units, and a culture that celebrates risk-taking and rapid action.

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**I**N CONTRAST TO INDUSTRIES like media and retail, where digital technology has been a significant disruptive force, process-oriented industries such as energy, transportation, industrial goods, and health care have not yet seen its full effects. (See Exhibit 1.) For management teams in these industries, it can be difficult to know how to start implementing digital technology—or even to see the need.

### EXHIBIT 1 | Industries Are at Different Stages in the Adoption of Digital Technology



Source: BCG analysis.

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Late adopters need to embrace the concept of “fail fast and fail cheap” and build up their digital capabilities through direct experience.

As a result, many companies have yet to take action to capitalize on digital. Some of these late adopters say they are hindered by legacy IT systems or don't have the necessary capabilities in place. Others spend months studying the market and getting bogged down in large-scale strategic and conceptual considerations, believing—incorrectly—that they need to understand how and where the journey will end before they can take the first step. The development cycles of digital technology are extremely rapid—far faster than for most traditional products and services—and this deliberate (and outdated) approach means that these companies are essentially fighting yesterday's battles.

Given the pervasiveness, low cost of entry, and potential impact of digital technology, it's imperative that late adopters act today to launch new digital products and services and digitize internal processes. This means they must implement far more nimble development processes and become far more comfortable making decisions amid uncertainty. Rather than using a top-down, strategy-driven approach (which worked in the past), these companies need to innovate using build-assess-learn cycles, even when not entirely sure of the outcome. They need to focus on pilot tests and prototypes that can be developed and rolled out quickly, assessed for performance, and scaled up (or shut down) accordingly. They need to embrace the concept of “fail fast and fail cheap” and build up their digital capabilities through direct experience. And rather than making a single big, strategic bet, they need to manage multiple initiatives, trying out new business models with low sunken costs, killing off the losers, and scaling up the winners.

Our experience with companies in virtually all industries shows that success with this kind of trial-and-error approach requires a structured transformation methodology built around three steps: securing quick wins at the outset, scaling up successful initiatives, and leading and sustaining change. (See the sidebar “Three Stages of a Digital Transformation.”) Together, these steps can help management teams determine where to start, how to manage the process, and how to generate sustainable progress with their digital transformations. (See Exhibit 2.)

## Securing Quick Wins at the Outset

Companies seeking to pursue digital often proceed from very different starting points, with different capabilities, circumstances, and degrees of ambition. Some will require a full transformation of their operations, processes, and business model in order to fully leverage digital technology and drive revenue. Others may only need to increase efficiency by reengineering their existing business and operating models.

Regardless of how ambitious their digital effort, companies should start with quick wins in at least one of several areas: improving the customer experience, offering new digital products and services, and digitizing internal processes.

To improve the customer experience, some energy companies are starting to offer mobile apps that allow customers to check bills and obtain meter data. More advanced offerings from retail chains allow customers to keep track of shopping lists and order out-of-stock items through an e-commerce portal on their smartphone. (See the sidebar “A Retail Player Quickly Rolls Out a Mobile App.”) Similarly, some

## THREE STAGES OF A DIGITAL TRANSFORMATION

BCG has helped clients in all industries launch transformations across a range of functions and disciplines. Based on that work, we have developed a three-part methodology:

- Launch quick wins that generate financial results in 3 to 12 months, free up capital for the overall effort, and establish momentum.
- Win in the medium term by developing the business model and operating model to increase the company's competitive advantage and fend off new entrants.
- Lead and sustain performance by building capabilities and designing the organization to build on performance gains over time.

In a digital transformation, these steps are slightly modified. The process still starts with quick wins, but they are aimed at rapidly developing new digital products and services and improving the customer experience (rather than freeing up capital to fund a longer journey). The second step in a digital transformation is to scale up the most successful digital initiatives and fit them into the organization in the right way. And the third step is similar: leading and sustaining improved performance over time. (See *Transformation: The Imperative to Change*, BCG report, November 2014, and *The New CEO's Guide to Transformation: Turning Ambition into Sustainable Results*, BCG Focus, May 2015.)

travel sites send flight status updates, departure gates, seat assignments, rental car confirmations, hotel directions, and other trip-related information to customers' phones—all sequenced to arrive at precisely the right time. And automakers are improving sales by using digital channels to send vehicle information and specs to potential customers at critical junctures in the purchasing process.

The second source of quick wins is new data-driven offerings and services that complement the company's existing assets and business model. These offerings don't merely improve the value proposition for customers; they transcend it and help the company expand into new areas of the value chain. For example, many banks are moving beyond the processing of payment transactions into services such as shopping, product comparisons, discounts, and post-transaction ratings. Similarly, telecom companies are starting to provide streaming-video and e-commerce services for their customers, in addition to basic voice and data. (See the sidebar "A Telecom Company Evolves from Network Operator to Digital Service Provider.") In the industrial goods industry, many companies are now using embedded sensors in capital equipment to warn users of maintenance issues, allowing them to make less expensive repairs early on and prevent larger problems.

The third option is to use digital to improve internal processes and functions, such as finance or HR. This approach is particularly relevant for B2B companies, which place less emphasis on the customer experience. The use of digital can improve the efficiency and accuracy of internal processes, reduce costs, and allow the company to use data-driven analytics to improve performance over time.

## EXHIBIT 2 | Specific Tools Used in the Three Steps of a Digital Transformation



### 1. SECURE QUICK WINS

Launch new products and services through MVP prototypes

- Get products to market quickly
- Refine them based on customer feedback
- Limit investment in time and capital
- Develop a mind-set of experimentation through trial and error



### 2. SCALE UP SUCCESSFUL INITIATIVES

Acquire digital talent through outsourcing and then build up internal capabilities

- Access a nucleus of external digital talent on a transaction basis
- Embed those capabilities internally over time
- Form a specialized digital team (akin to a center of excellence)
- Deploy talent from that unit into other departments and functions to build digital capabilities across the organization



Create a start-up incubator through a joint venture or partnership with another company

- Tap into external expertise and capabilities
- Develop a start-up mentality
- Fund external companies in exchange for a share of the upside (as well as to build up internal capabilities over time)
- Limit risks from the new venture for existing operations



### 3. LEAD AND SUSTAIN CHANGE

Adopt strong change management processes for digital ventures

- Sustain momentum through a longer-term approach to digital technology
- Generate support from leaders
- Foster collaboration across functions and business units
- Establish the right model for IT

Source: BCG analysis.

Whether a company begins its digital transformation by improving the customer experience, developing new products and services, or improving internal processes (or a combination of all three), speed is critical. Instead of taking the traditional, linear approach to rolling out new initiatives, companies should quickly bring new ideas to market, gather customer feedback, and refine the concept iteratively. Many accomplish this by means of the minimum viable product (MVP) process of prototyping.

The MVP process is based on the idea of the “good enough” product. Rather than trying to perfect new products or services internally during the development stage, the company instead aims to get them to market quickly, with just enough features included to make them functional. That allows the company to minimize its investment, test the new products and services in the real world (instead of in artificial settings such as focus groups), and refine them using customer feedback. For example, the initial versions of apps and online stores are often quite basic, with new features and functions added over time, depending on how the products are used by customers.



## A RETAIL PLAYER QUICKLY ROLLS OUT A MOBILE APP

A multinational big-box retailer operating in an emerging market launched a quick-win initiative with a mobile app to boost declining sales at its physical stores. Rather than develop a grand digital strategy or conduct detailed market research to determine the scope of the opportunity, the retailer outsourced the entire app-development process so it could get something to market quickly.

The app included customer-friendly features like personalized coupons and offers, tools to plan shopping trips, automatic replenishment of regular purchases (though a subscription model), and in-store navigation. It resonated strongly with customers and led to increased sales at the retailer's stores, especially once management learned what worked well and continued to add new features, such as

in-store WiFi and home delivery of goods purchased online.

The overall initiative was so successful that the retailer extended the outsourcing arrangement for a second year, meanwhile hiring digital talent and building up its own internal capabilities in critical areas, such as customer analytics, mobile payment processing, app development, and coding. Eventually, it rebuilt the main app using internal resources and continued to refine and improve it over time. By outsourcing much of the process initially, the company was able to get an app in consumers' hands quickly, build its digital capabilities over time, and learn from direct experience.

## A TELECOM COMPANY EVOLVES FROM NETWORK PROVIDER TO DIGITAL SERVICE PROVIDER

A telecom company that dominated its home market recognized the risks of commodification early. It knew that focusing on voice and data networks put it in danger of becoming a mere conduit for information, while digital start-ups built innovative mobile services that customers would access (and pay for) through its wireless network. To capture some of this emerging revenue in digital, the company began to leverage its wireless network to offer new services.

For example, the company developed a mobile payment service, a streaming-movie offering, and health care apps. A consistent theme across all

these new services was that they served as platforms that other mobile developers could build on; that is, rather than building walled-off, proprietary services, the telecom developed an ecosystem that others could use to create even richer offerings. Yet the telecom retained control of the customer relationship, along with payment and authentication services. As a result, it had immediate access to customer data, which it could use to refine and improve its offerings.

Ultimately, the company revamped its IT platform to support the new service-based approach, and revenue from services grew dramatically.

## Scaling Up Successful Initiatives

Once the company has identified its most important digital priorities and launched some quick wins, it faces the challenge of scaling up the most promising ventures. Several levers are available to accomplish this. The right one depends on the company's level of ambition, the strength of its existing digital capabilities, and external market factors (primarily, the degree of disruption posed by new digital competitors).

The fastest way to scale up digital initiatives is to acquire digital talent on a temporary basis and then bring it in-house over time. As the company embeds talent, it can create digital units that serve as a center of excellence and an internal repository of its current thinking on technology. This is an iterative and incremental model that allows the company to develop digital capabilities organically. Redesigning business processes in this fashion takes time, but it allows the company to develop its own expertise. Critically, success often requires new leadership positions, such as a chief digital officer.

A second, and bolder, approach is to create an internal incubator to leverage capabilities already developed by another company—preferably, an entrepreneurial one. This can be done through early-stage funding of start-ups (the corporate venture-capital model), a joint venture, or an outright acquisition. (See the sidebar “An Insurer Creates a Joint Venture to Enter a Challenging Market.”) Regardless of the ownership structure, the company takes an active role by investing in and develop-

### AN INSURER CREATES A JOINT VENTURE TO ENTER A CHALLENGING MARKET

A global insurer wanted to enter a fast-growing Asian market, but several initial efforts had failed. The company then developed a joint venture that would enter the market through a “Trojan horse”—a noninsurance product marketed under a new brand name.

Aware that a potential new demographic for insurance was pregnant women and new mothers, the company developed a digital device that pregnant women could wear to monitor the heartbeat of the fetus. The joint venture was staffed with a combination of employees at the insurance company and new hires who provided the needed digital capabilities, and it rolled out the product using quick, iterative cycles and customer feedback on prototypes.

In addition, the company created a website where women could monitor heartbeat data and exchange information with other expectant mothers. (Family members could also log on.) The site included original content from medical experts, and it was open to participation by other companies offering wearable technology. This approach allowed the insurer to establish a foothold in the market, which it then used to cross-sell its insurance products.

Critically, the joint venture was completely separate from the parent company, with different governance, financials, and technology. This allowed it to move fast and operate like a start-up, free from any institutional inertia on the part of the parent company.

ing the new entity, with the goal of cultivating digital capabilities that it can harness—and potentially bring in-house. This approach allows the company to move quickly into digital and build a start-up mentality while limiting the risk of failure and the impact on existing operations. However, it requires capital, the willingness to act like an investor, and the right degree of oversight.

## Leading and Sustaining Change

The third step in our digital transformation methodology requires the right set of internal resources. Even successful pilot projects and prototypes will not achieve their potential without organizational support. Companies need to nurture these projects to make sure they become sustainable at scale.

Most important is leadership. The company's digital agenda needs to be driven by executive management, with visible support and accountability. (Bottom-up approaches usually do not last.) Talent and culture are critical as well. The company must hire high-potential employees with skills in such areas as agile development and analytics. And it must build a "venture" culture within both the business units and IT—including a trial-and-error mind-set that not only tolerates failure but understands that failure is a critical part of the process. In this effort, HR should work closely with the business units.

The company also needs to determine how IT can best support its digital initiatives and whether to house its digital capabilities within the business units or in a corporate center of excellence (either within or outside the company). Many companies opt to deploy dedicated new-technology platforms—particularly for customer- and analytics-focused initiatives—which function separately from the core IT department and have their own databases and other infrastructure. Digital initiatives require different capabilities and entail much faster development cycles, and they often benefit from having a clear place in the organization, along with dedicated resources. (See the sidebar "An Auto Manufacturer Uses a Two-Speed IT Structure to Support a Digital Initiative.")

Many companies also need to break down institutional barriers and silos in order to foster a more collaborative approach between IT and the business units. Cross-functional teams put more eyes on each initiative, allowing problems to be rooted out early and promising ideas to be pushed out to market faster. (See the sidebar "A Global Bank Revamps Its Organizational Model.")

Finally, companies should adopt strong change-management processes. A key challenge is meshing digital initiatives with the company's established operations and ensuring that employees and managers on both sides continue to collaborate so that digital successes can spread throughout the organization. At the same time, even failures present an opportunity to learn.

## How to Move Forward

Before a company can begin its digital journey, it needs to assess its readiness by looking at the availability and quality of data, its IT architecture (including the de-

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The company's digital agenda needs to be driven by executive management, with visible support and accountability.

## AN AUTO MANUFACTURER USES A TWO-SPEED IT STRUCTURE TO SUPPORT A DIGITAL INITIATIVE

A multinational automobile company wanted to use digital technology to improve its sales cycle. The management team studied the car-buying process and identified several “moments of truth” when customers were turning away rather than continuing to engage. Market research indicated that the company could improve sales by reaching out to customers through digital channels at those junctures, with more targeted marketing messages, vehicle specifications, and other information intended to win customers over. An early-stage, four-month test based on external technology was successful, but the company realized it

didn't have the right internal IT structure in place to roll out the new communication model. It therefore split its IT function in two: one section would support the company's existing operations using traditional legacy systems, while another would move faster to develop cloud-based mobile technology and other digital tools that could support the new initiative. With the two-speed IT structure in place, the automaker would be able to roll out the new communication model across the entire company.

## A GLOBAL BANK REVAMPS ITS ORGANIZATIONAL MODEL

With digital innovators increasingly influencing customer expectations, a global bank embarked on an internal transformation with three objectives:

- Allow the bank to respond faster to changing customer requirements
- Increase efficiency by breaking down organizational silos and bureaucracy
- Increase staff engagement and make the bank more attractive to digital talent

Drawing inspiration from innovative digital companies, the bank reorganized into mini-start-ups, with employees from marketing, product development, customer intelligence, digital channels, and IT working together in small, multidisciplinary, colocated

teams. The teams were empowered to develop, test, deploy, maintain, and adapt customer processes and propositions according to their specific mandates. At the same time, the bank adopted a new governance system that ensured that the teams were aligned with the company's larger business objectives.

In addition, the traditional manager's role was replaced by product owners, expertise leaders, and agile coaches geared to building high-performance teams. This enabled the bank to reduce management layers and workforce size in functions like marketing, product management, and digital channels by more than 30 percent. At the same time, the bank attracted new talent from digital innovators outside the company to strengthen its internal capabilities in the most critical areas.

gree to which it is digital-ready), its capabilities in innovation, and its overall culture and readiness for change.

Talent is a critical element—management teams should work with HR to evaluate the company’s pool of digitally skilled employees, including those in areas such as programming, mobile, IT implementation, digital marketing, social media, and data analytics.

In addition, the company should understand its competitive environment, meaning current trends in digital that are affecting its industry (or are likely to have an effect in the next several years), along with the digital capabilities of competitors. This need not be a comprehensive, exhaustive process. Rather, the entire assessment should take four weeks at most. As with all digital endeavors, speed and initiative are critical. Launching quick-win initiatives based on partial information is far better than trying to complete a precise assessment before taking a first step.

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