From disrupted to disruptor: Reinventing your business by transforming the core

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Companies must be open to radical reinvention to find new, significant, and sustainable sources of revenue.

When Madonna burst onto the scene in the early 1980s, there was little reason to suspect that she'd have more than her allotted 15 minutes of fame. But in the three decades since her debut album, she has managed to remain a media icon.

Her secret? "Madonna is the perfect example of reinvention," Janice Dickinson, renowned talent agent, has said. Fittingly, the name of Madonna's sixth concert tour was "Reinvention."

Madonna may seem like an unlikely touchstone for modern businesses, but her ability to adapt to new trends and set some others offers a lesson for companies struggling with their own digital revolutions. That's because the digital age rewards change and punishes stasis. Companies must be open to radical reinvention to find new, significant, and sustainable sources of revenue.

Incremental adjustments or building something new outside of the core business can provide real benefits and, in many cases, are a crucial first step for a digital transformation. But if these initiatives don't lead to more profound changes to the core business and avoid the real work of rearchitecting how the business makes money, the benefits can be fleeting and too insignificant to avert a steady march to oblivion.

Simply taking an existing product line and putting it on an e-commerce site or digitizing a customer experience is not a digital reinvention. Reinvention is a rethinking of the business itself. Companies need to ask fundamental questions, such as, "Are we a manufacturer, or are we a company that enables customers to perform tasks with our equipment wherever and whenever they need to?" If it's the latter, then logistics and service operations may suddenly become more important than the factory line. Netflix's evolution from a company that rented DVDs to a company that streams entertainment for a monthly subscription to one that now creates its own content is a well-known example of continuous reinvention.

Reinvention, as the term implies, requires a significant commitment. From our Digital Quotient® research, we know that digital success requires not only that investment be aligned closely with strategy but also that it be at sufficient scale. And digital leaders have a high threshold for risk and are willing to make bold decisions.[1] But companies don't have to wait far in the future to realize those benefits. We've found that 60 to 80 percent of total improvement targets can be achieved within about three years while also laying the foundation for future growth.

For all the fundamental change that digital reinvention demands, it's worth emphasizing that it doesn't call for a "throw it all out" approach. An engine-parts company, for example, will still likely make engine parts after a digital reinvention, but may do so in a way that's much more agile and analytically driven, or the company may open up new lines of business by leveraging existing assets. Apple, with its move from computer manufacturer to music and lifestyle brand through its iPhone and iTunes ecosystem, reinvented itself—even as it continued to build computers. John Deere created a whole series of online services for farmers even as it continued to sell tractors and farm equipment.

There are many elements to a transformation, from end-to-end journey redesign and embedding analytics into processes to open tech platforms. They require a myriad of capabilities, from artificial intelligence and agile operations to data lakes, cloud-based infrastructure, and new talent. Many of these elements have been written about extensively, and each can absorb a significant amount of executive time. What's often missing, however, is a comprehensive view of *how* an organization sets the right ambition, *how* to architect the right elements for the transformation, then *how* to systematically and holistically undertake the change journey.

1 "Raising your Digital Quotient," *McKinsey Quarterly,* June 2015, McKinsey.com.

What the ‘core’ is and why it needs to change

“Think of your core muscles as the sturdy central link in a chain connecting your upper and lower body.”[2] That was the guidance from Harvard Medical School on how to stay in shape. The authors defined the core as the central set of muscles that helps a body maintain its power, balance, and overall health.

That’s the essence of what we mean when we talk about changing the core of the business—the set of capabilities that allows the entire business to run effectively. A company’s core is the value proposition of its business grounded in strategy as enabled by its people, processes, and technology. These elements are so intrinsic that any transformation that doesn’t address them will ultimately underwhelm and fizzle because the legacy organization will inevitably exert a gravitational pull back to established practices.

Value proposition: Any digital reinvention must address the value the company provides to customers (whether existing or new) through its products and/or services. Inevitably this is based on a clear strategy that articulates where value is being created, shifted, or destroyed. Crucial to getting this right is identifying and evaluating existing assets that are most important and understanding what customers actually want or need. This can be surprisingly difficult to do in practice. The value that Amazon originally provided, for example, wasn’t selling books online but rather providing convenience and unheard-of selection. Understanding the real source of its value allowed Amazon to expand exponentially beyond books.

People: Of course talent is important, but a reinvention needs to involve more than just hiring a CDO or a few designers. Talent priorities should be based on a clear understanding of the skills needed at all levels of the business. This requires investing in building relevant digital capabilities that fit with the strategy and keep pace with customers as they change the way they consider and make purchases. At the same time, targeted hiring should be tied to those capabilities that actually drive financial performance. (For more on talent, please read “Raising your Digital Quotient,” on McKinsey.com.)

Enabling that talent to thrive requires a digital culture, i.e., one that is customer centric and project based, with a bias for speed and continuous learning. In fact, cultural and organizational issues can lead to the squandering of up to 85 percent of the value at stake.[3] Making sure the new culture sticks requires rebuilding programs that reward and encourage new behaviors, such as performance management, promotion criteria, and incentive systems.

2 “The real-world benefits of strengthening your core,” *Harvard Health Publications*, Harvard Medical School, January 2012.

3 2016 Digital McKinsey Survey.

Processes: Rewiring the mechanisms for making decisions and getting things done is what enables the digital machine to run. Digitizing or automating supply chains and information-intensive processes as well as building new capabilities like robotic process automation or advanced analytics, for example, can rapidly increase the business's clock speed and cut costs by up to 90 percent.[4]

One temptation is to focus on simply digitizing existing processes rather than really rethinking them. Often, the most productive way to tackle this issue is to identify the customer journeys that matter most to the business and then map out the touchpoints, processes, and capabilities required to deliver on them—without regard to what is already in place. Rearchitecting processes requires establishing governance and decision rights to provide clarity and accountability, as well as embedding advanced analytics, automation, and machine-learning capabilities. (For more, please read "Accelerating the digitization of business processes," on McKinsey.com.)

Technology: While digital reinvention is more than just a technology overhaul, technology is crucial to it. Leaders need to ensure that each IT investment responds to clear and robust business needs, and does not devolve into "tech for tech's sake." They also need to identify how best to work within an ecosystem of partners and vendors, and assess which legacy systems to keep, which to mothball, and—critically—determine how to help legacy technology work in a digital world.

Reinvention requires a proven, systematic approach

Because of the complexity involved, most reinventions fall short of their original goals. In our experience, extracting the full value from digital requires a carefully coordinated approach across four "Ds": Discover what your digital ambition is (based on where the value is); Design programs that target profitable customer experience journeys; Deliver the change through an ecosystem of partners; and De-risk the process by thoughtfully sequencing steps (exhibit).

While this approach may seem self-evident, we find that most companies fall short in the execution. There are myriad reasons for this, but the most common are that the business either underinvests in the capabilities needed or doesn't drive the transformation program sufficiently across all four of the "Ds." A company may invest tens of millions of dollars to "Discover" great insights, for example, but if its "Deliver" strategy is inadequate, those insights are for naught.

1. Discover: Shape your digital ambition, strategy, and business case

In this phase, companies develop a clear view of where value is being created and destroyed as the basis for a clear business strategy. That requires an analysis of their business, sector,

4 Shahar Markovitch and Paul Willmott, "Accelerating the digitization of business processes," March 2014, McKinsey.com.

EXHIBIT

The 4Ds of a digital transformation

Discover: Shape digital ambition, strategy and business case based on insights

Design: Reinvent and prototype new capabilities and breakthrough journeys as part of a program

Deliver: Activate an ecosystem to rapidly deliver at scale

De-risk: Structure the change program, resources and commercial model to reduce operational and financial risk

customer-behavior trends, and the larger economy to identify and quantify both threats and opportunities. These kinds of digital opportunity scans should be sorted by short- and long-term pockets of value. (For more on this, please read "The economic essentials of digital strategy," on McKinsey.com.)

At the same time, companies need to engage in a sober analysis of their own digital capabilities and resources. Capabilities that build foundations for other key processes and activities (e.g., modular IT and agile technology platforms) are particularly important. And while leadership matters, our DQ™ research has shown that midlevel talent is the most critical element for a company's digital success.

With this understanding in hand, companies then determine what their strategic ambition is, whether retooling the existing business or something more radical, such as plunging into a new market or innovating a business model. They develop a detailed road map for addressing capability gaps, and recruiting, developing, incentivizing, and retaining the necessary talent. The goal is to develop a tight business case for change based on facts.

2. Design: Create and prototype breakthrough experiences

Actually acting on a digital ambition can be daunting. We have found that the most successful companies start by focusing on the most important customer journeys, then work back from there to design and build out breakthrough customer experiences. Using design thinking and skills, these companies define each journey, looking especially for the pain points and potential missed connections. The change team can then map out, screen by screen, models for a new interface. In this phase, the company must avoid getting caught in endless rounds of planning but instead rapidly build prototypes, translating concepts into minimum viable products to test and iterate in the market before scaling.

This phase also includes building out rapid delivery approaches and an IT infrastructure that blends the legacy systems with microservices and modular plug-and-play elements). While agile IT has become standard, more digital businesses are embracing DevOps (integrated development and operations teams) and continuous delivery so that software can be developed, tested, and deployed quickly to consumers and end users.

On the organization side, the fluid nature of cross-functional collaboration, rapid decision making, and iterative development means that the business should focus on the enablers for this kind of teamwork. These include effective metrics and scorecards to evaluate digital performance and incentive structures to drive the right behaviors, mind-sets and outcomes. The CDO at one multinational pharma company addressed this issue by establishing a "digital council," which was tasked specifically with breaking down organizational silos to enable transformational change across all business lines. The initiative was credited with significantly contributing to a 12 percent increase in sales.

3. Deliver: Develop a network of partners who can rapidly scale your ambition

Getting the speed and scale necessary for a reinvention increasingly requires an ecosystem of external teams, partners, suppliers, and customers. In practice, this means working with a mix of platform players, delivery specialists, and niche players. These are the relationships that companies can call on to provide specific skills and capabilities quickly.

This reality has made ecosystem management an important competency, especially understanding how to find and plug into the right mix of complementary capabilities. One national bookseller, for example, built out a digital offer by partnering with a telecom company for its technology and with a range of retailers to build up a marketplace. This approach allowed it to rapidly hit the marketplace and increase revenue 78 percent in a year.

As companies push to scale their digital reinvention throughout the organization, the crucial role of seasoned change managers comes into focus. These leaders not only play "air traffic controller" to the many moving parts, but also have the business credibility and skill to solve real business problems. They must maintain an accelerated pace of change and drive accountability across the business. The change leaders will look across the entire enterprise, examining organizational structure, data governance, talent recruitment, performance management, and IT systems for areas of opportunity, making decisions that balance efficiency and speed with outcome.

The “agility coach” is an example of this type of role. This person has strong communications and influencing skills, can create and roll out plans to support agile processes across the business, and can put in place KPIs and metrics to track progress.

4. De-risking: Structuring the process to minimize risk

One of the most common reasons digital transformations fail is that the organization develops “change exhaustion” and funds start to dry up. To mitigate this risk, it’s important to focus on quick wins that not only build momentum but also generate cost savings that can be reinvested in the next round of transformations. One global e-tailer, for example, focused on quick wins (such as increasing conversion rates) and was able to deliver $350 million in new revenue in just five months, which funded further changes and provided tangible results to further excite the business about the journey. This sequencing approach applies to tech as well. Many companies choose to invest first in “horizontal” components, such as business-process management (BPM) layers or central administration platforms that can be shared across many initiatives, while balancing them with more “visible” elements to provide the proof of concept.

Technology risks, especially cybersecurity, will also require increased attention as companies digitize more operations and processes. Organizations can mitigate these risks by automating tests on software, establishing systems in which failures can be rolled back in minutes, and establishing build environments in which fixes can be made without putting significant parts of the business at risk. Senior leaders in particular need to focus on the structural and organizational issues—from building cybersecurity into all business functions to changing user behavior—that hamper the ability to manage cyber risk.

One risk senior leaders often overlook is losing ownership over sources of value. These might include the company’s data, customer relationships, or other assets. Having a clear understanding of where the value is coming from allows businesses to navigate ecosystem relationships profitably. In evaluating which partners to work with, the bookseller mentioned above, for example, declined to work with a storefront partner because it feared losing its most valuable asset: its direct relationship with its customers.

Digital reinvention will put new demands on leadership. Here are some crucial questions leaders should ask themselves:

- Where have our past transformations succeeded or broken down?
- What do our customers say about their experience with our company?
- Do we understand what the next sources of value are and are we ready for them?
- Are we investing in the right places and at the right levels to reinvent ourselves?

Companies can both rise and fall with astonishing speed as new customer needs are uncovered and new ways of meeting them are developed. We strongly believe that companies that are able to adapt, learn, and find new solutions quickly can do more than just retain market position; they can thrive, whatever disruptions come their way. As Madonna once said: “You have to reinvent to stay in the game.”

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