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Six lessons on how to embrace the next-generation operating model

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Realities on the ground highlight what's really needed to pull off the transformation.

Companies that hope to compete in the digital world are coming to see that it requires a fundamentally new way of working. On the customer-experience side, digital natives have raised the bar considerably; for example, banks today benchmark their websites and apps against companies such as Amazon and Uber. Internally, despite big investments in digitization, process redesign, and automation, the efficiency ratio at most large companies has stalled. Their improvement initiatives reside in different pockets, such as a digital factory or automation center of excellence, and are seldom integrated.

A next-generation operating model¹ (NGOM) is needed to give companies the ability to move quickly and adapt to changing circumstances. The rewards for making the leap to the NGOM are significant: step-change improvements that produce 30 to 50 percent productivity gains, up to 80 percent reduction in turnaround time, up to 10 percent enhancement of customer experience, and 20 to 25 percent growth.

Last year, we identified the two key shifts that are necessary for companies to build the NGOM:

¹ For a compendium of articles on the next-generation operating model, see "Introducing the next-generation operating model," March 2017, McKinsey.com. For an overview of the model, see Albert Bollard, Elixabete Larrea, Alex Singla, and Rohit Sood, "The next-generation operating model for the digital world," March 2017, McKinsey.com.

From uncoordinated improvement efforts within siloes . . . **To** an integrated transformation program organized around customer journeys (the interactions a customer has with a company) and internal journeys (end-to-end processes inside the company).

From using individual technologies and capabilities in a piecemeal way inside siloes . . . **To** applying them to journeys in combination and in the right sequence, thereby achieving compound impact.

Over the past couple of years, as we've worked with companies to develop their NGOM, six important lessons have emerged.

Lesson #1: Start by working on a high-impact end-to-end journey

Some companies start their digital operations transformation with small pilots that don't generate significant benefits. Others spend a lot of time analyzing which journey to tackle first. But there's no single right way to get started. The key is to identify a journey that's important and begin there.

There are two primary approaches for deciding where to begin:

- If a “burning platform” at the company is already in mind—an issue with potential to have a big impact on customer experience, new-customer acquisition, customer service, and/or cost/productivity—simply start there. Alternatively, identify no-regret areas (every company has a few) and pick one. Set up a cross-functional, agile team to tackle the chosen area.
- If there are several burning platforms, evaluate the potential of the next-gen levers across the most important customer journeys at the enterprise level. This will help prioritize and sequence journeys for the next two to three years after embarking on the transformation.

Whichever path is chosen, it's important to get started quickly in order to demonstrate the *from-to* path for the next-gen transformation and win over skeptics by showing the value the model can generate. We have found that it's generally better to take on customer-facing journeys before internal ones. If it's hard to get the buy-in needed to begin with a whole journey, it's possible to start smaller—inside a single business unit or geographic site—and later extend the effort to include the entire journey from end to end.

Companies have started with a range of high-impact journeys. A North American bank began with home-mortgage origination on an end-to-end basis. For a global property-and-casualty insurer, the starting point was policy services; for a credit-card issuer, it was customer acquisition; for a life insurance issuer, it was new-business origination; and for an airline company, it was the ticket and ancillaries sales journey. Companies in other industries have also applied the NGOM, starting with journeys such as production of steel or restocking of store shelves. Despite beginning in quite different places, all of these companies experienced comparable results along key dimensions that drive costs and revenue growth.

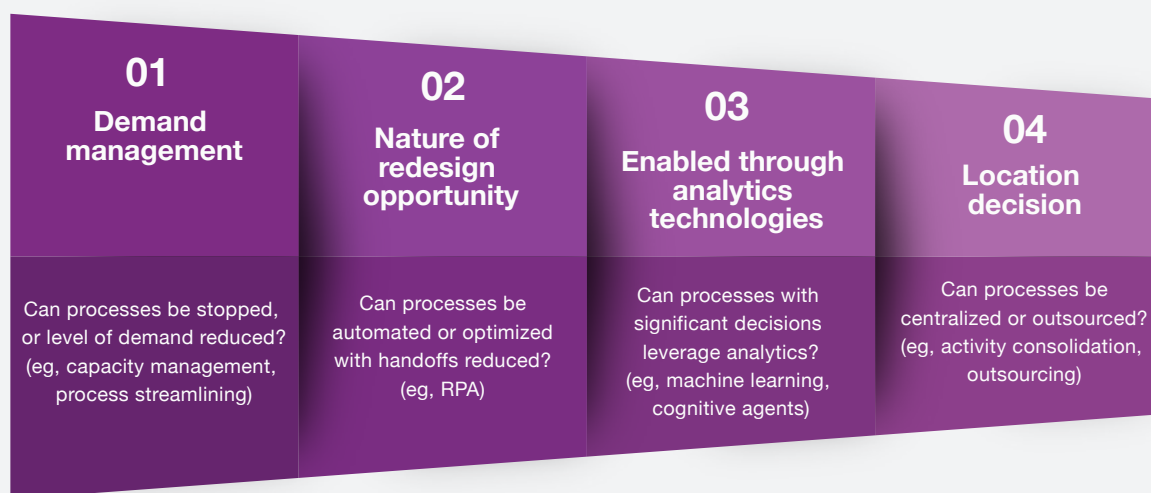
Lesson #2: Be systematic when prioritizing and sequencing improvement levers

The NGOM integrates multiple improvement levers—process redesign, digitization, automation, analytics, and outsourcing/offshoring—to achieve step-change improvements. Yet there can be complex interdependencies between levers. In some settings, for example, applying robotic process automation (RPA) before redesigning the process can be a waste of time. It's critical to understand the interdependencies and to be systematic in selecting the mix and sequence of levers.

Use a structured process to understand the potential of the key levers and the dependencies between them.

Understanding interdependencies between levers helps to achieve improvements.

Example of how a company goes through selection and sequencing of improvement levers



These can vary depending on such factors as the journey being addressed or location (exhibit).

A vehicle-leasing company recognized there were significant differences in the level of sophistication of its operations in different countries, which meant the applicability of levers varied widely. In one country, where capabilities are less mature, it plans to implement a major process-redesign effort and then centralize key activities, all as a prelude to introducing automation. In another country, by contrast, where the processes are more mature, centralization will be the first step, followed by automation. Another strategy the company is keeping in mind is to favor early initiatives that can generate short-term return on investment.

Lesson #3: Apply the next-generation operating model across all steps of core journeys to get the most value

Often, companies start by applying the NGOM in a focused way—for example, to a customer-facing journey in the organization’s front end. But achieving

step-change improvements from the NGOM requires applying it from the point where the customer interacts with the brand all the way through to the back-end systems that support and deliver on that interaction. At most companies, 20 end-to-end journeys account for more than 70 percent of the costs and more than 80 percent of the customer experience. Transforming core journeys touches all parts of an organization and requires spanning “horizontally” to cut across silos and deliver step-change, multidimensional improvements.

We have observed two approaches that can extend the NGOM horizontally:

- The most common is to start at the front end, with the customer-facing aspects of a journey, and later extend the effort to internal processes housed in the back office.
- A more aggressive approach is to begin working horizontally from the outset, by assigning responsibility for all aspects of customer-facing

journeys, and the key internal processes that support them, to cross-functional agile squads. In this approach, organizational change happens before journey transformation.

One other important way to realize true impact from end-to-end journey transformation is by creating a new role: the journey owner, who has the authority to call on resources from the multiple groups that must contribute to delivering on that journey. In a bank, these could include the front, middle, and back office, as well as IT, risk, and compliance. Because the end-to-end journey owner must engage with many parts of the organization, it is a challenging role and should be filled by a highly capable executive. The end-to-end journey owner should report to a C-level executive: chief digital officer, COO, or even the CEO.

A leading global financial-services company wanted to improve its customer-exception journey. To break down silos within the business, it started by standing up a cross-functional team with process redesign, agile, digital, and automation expertise and representation from compliance, legal, risk, and privacy. The team then focused on improving the entire customer journey. To enhance the customer experience, it tackled the front end by digitizing its customer self-service portal and improving existing interactive voice response (IVR). In parallel, it redesigned processes to drive efficiency in the back office, enabling future RPA opportunities. This “horizontal” approach, spanning multiple parts of the organization, is on pace to deliver close to a 20 percent reduction in cost of service delivery, a more than 35 percent improvement in work efficiency and quality of service, and a more than 20 percent gain in people-engagement scores.

Lesson #4: Start on the talent challenge immediately

Most companies do not fully grasp their talent challenge. Not only do they need new skilled people, but they also need to reskill or redeploy existing staff, since certain improvement levers, such as RPA, will replace some jobs and transform many others.² Because these challenges don’t appear immediately, companies tend not to focus on them until it’s too late, at which point talent management becomes a bottleneck on their path toward the NGOM.

Organizations need to start preparing right away to get the talent needed for the future workforce. The first step is to assess future skill demand in key areas such as data science and agile, diagnose the current supply, and launch initiatives to fill the gap. This requires HR to work closely with the executives in charge of implementing the NGOM to gain a complete understanding of what the real skill needs are.

Reskilling and redeploying staff is a critical step in monetizing the value generated by the next-generation operating model.³ For example, a data-entry analyst whose former work is automated could be upskilled to oversee RPA systems. It’s worth noting that not everyone can be reskilled to the roles in greatest demand; a call-center rep can’t be trained in a few months to become a data scientist or an agile scrum master.

A global bank set up a digital factory in a new facility in its home country’s leading tech region, plus satellite digital factories in the tech centers of four countries where it had subsidiaries. It built out the offices so they resembled start-ups

² Research by the McKinsey Global Institute notes that rather than replacing entire jobs wholesale, new technologies will more often be used to undertake some of the *activities* that are a part of current jobs. See James Manyika, Susan Lund, Michael Chui, Jacques Bughin, Jonathan Woetzel, Parul Batra, Ryan Ko, and Saurabh Sanghvi, “Jobs lost, jobs gained: What the future of work will mean for jobs, skills, and wages,” McKinsey Global Institute, November 2017, on McKinsey.com.

³ For more on value capture, see Pooneh Baghai, Somesh Khanna, Eric Lamarre, Asheet Mehta, and Mateen Poonawala, “Banks and the digital flywheel: An engine for ongoing value capture,” July 2018, McKinsey.com.

and established partnerships with university research centers and early-stage fintechs to create a collaborative environment that leveraged the new offices' locations inside larger tech ecosystems. Its recruiting materials emphasized that positions in the digital factory were anything but typical banking jobs.

Lesson #5: Don't let technology debt scare you off

Many companies are in technology debt and believe they cannot achieve the full potential of the NGOM without fully revamping their IT architecture and systems. But no matter what the condition of their current infrastructure, companies can take advantage of the NGOM by making incremental tech upgrades along their transformation journey and so accrue significant benefits without needing to wait for a full system upgrade.

Companies have followed two paths in addressing their technology debt:

- The first involves building individual databases and applications, driven by specific use cases, separate from the existing legacy infrastructure. This creates new capabilities, which can then connect back with legacy systems on a case-by-case basis, using application programming interfaces (APIs) and microservices.
- Cloud and open-source technologies now make it affordable to build entirely new infrastructure, on a limited scale, to meet the emerging needs of the NGOM, while continuing to run existing legacy systems in parallel. As this new, clean stack grows over time, it can increasingly be used in lieu of the legacy infrastructure.⁴

A large financial-services firm launched an analytics initiative that relied on machine learning, along with associated digital tools and process redesign. When data from its digital customer-acquisition channels were fed into its existing infrastructure, the legacy systems effectively broke. In response, the company stood up new databases and analytics engines by deploying inexpensive cloud technologies and open-source tools. These systems worked well, and the company soon wanted to apply the new analytic models to its old data, which was housed in its legacy core. To make this work, the company wired the new systems and legacy core together with APIs and microservices. The company is now continuing along this path on a case-by-case basis, using the gains generated by earlier activities to pay for the next round of work.

Lesson #6: Keep evolving and adapting with continuous improvement

Our experience from transformation efforts has shown that the 80/20 rule applies. The initial big effort generates the majority of the value—the 80 percent. But the remaining 20 percent is still significant. Rather than stretch to “do it all” in one shot, find the 80/20 balance, and commit to continuous improvement to adapt and optimize the model.

To achieve the last 20 percent of value from the NGOM, a continuous-improvement mind-set should become the new “steady state.” That means making agile practices a way of life, not a project methodology, one that continually generates new ideas, prototypes them quickly, tests them to obtain feedback, and then iterates based on that input. Even after primary customer-facing journeys have been reconfigured, sizable productivity gains can still be achieved by tackling legacy operations and corporate

⁴ For more on how new technologies are allowing companies to stand up clean stacks at modest cost, see Michael Bender, Nicolaus Henke, and Eric Lamarre, “The cornerstones of large-scale technology transformation,” *McKinsey Quarterly*, October 2018, McKinsey.com

support functions such as finance and HR.⁵ The NGOM is not static. It must continually evolve and adapt.

At regular intervals—every three years or so—it’s also worth taking out a clean sheet of paper and reinventing with zero-based design.⁶

Conclusion: Embrace the journey

Adopting the next-generation operating model is a journey, and insights on how best to embrace it are evolving. We expect to learn more as the journey continues. But so far, these six lessons have consistently made a difference for the companies that applied them. ♦

⁵ For more on achieving productivity gains in legacy operations and corporate support functions, see Pooneh Baghai, Somesh Khanna, Eric Lamarre, Asheet Mehta, and Mateen Poonawala, “Banks and the digital flywheel: An engine for ongoing value capture,” July 2018, McKinsey.com.

⁶ For more on what zero-based design is, and how it works, see JP Higgins, Elixabete Larrea, Swapnil Prabha, Alex Singla, and Rohit Sood, “Why isn’t zero-based design delivering more value in improving customer journeys?” January 2019, McKinsey.com.

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