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WHEN TO SHIFT YOUR DIGITAL STRATEGY INTO A HIGHER GEAR

There may be a premium for making early moves.

by Jacques Bughin, Laura LaBerge, and Nicolas van Zeebroeck

When companies first sense a digital competitor entering their market space, they tend to react timidly, reasoning that the risk of damage to revenues and profits is not enough to justify tampering with current business models. Our research indicates, however, that executives may underestimate how close they are to an industry tipping point.[1]

The signals. As the exhibit shows, during the early stages of digital competition (when rates of digitization hover below 30 percent), fewer than one out of ten incumbent players across industries have adopted offensive corporate strategies that change their portfolios and business models.[2] At this juncture, new digital entrants typically hold less than 10 percent of the market. However, when industry digitization climbs toward the 40 percent mark, the environment changes abruptly. That's when digital attackers will likely have locked in a 15 percent market share and incumbents will be sensing that the upstarts have sufficient momentum to tilt the market to their advantage.

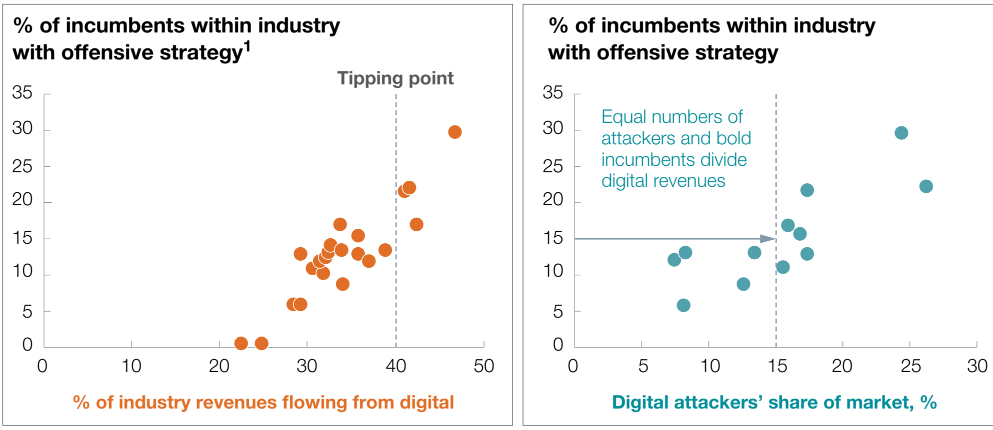
Many more incumbent players are reacting in ways that seemed unimaginable before. We found, for instance, that 15 percent of incumbent companies within an industry have revised their strategy—three times more than before the 40 percent threshold. As companies approach the 40 percent threshold, the portion of revenue digitized by incumbents still remains modest, just 20 percent, since they still have considerable legacy businesses. However, it's here that the two camps divide the market's overall digital revenues roughly evenly (15 percent for entrants and 17 percent for incumbents), so the risks of inaction are high.

The fallout. Mounting market turbulence hits digital laggards the hardest. Attackers squeeze their revenues, and heavy digital investments are now required to match what incumbent competitors are spending to play catch-up. Room for maneuver narrows substantially. Fast-moving incumbents, our research shows, still have a chance to stay in the game if they move boldly. However, companies in the bottom quartile of digitization will struggle to remain competitive.

We found that the high-tech, media, and telecom industries are well past the 40 percent digitization mark, with attackers taking more than a 15 percent share of the market, and in excess of one in five of incumbents moving boldly. Retail is

Exhibit

Incumbents' bold moves increase as the industry's rate of digitization rises and they respond to the growing market share of attackers.



[1] Specifically, strategies that place incumbents' revenue streams at risk with new digital offerings that reshuffle activities and current business models, and also strategies that significantly overinvest in digital technology relative to competition.

Source: Digital McKinsey survey, 2016

close to the tipping point with respect to digital entrants, although relatively fewer traditional companies are moving boldly. Incumbent healthcare-services players, on the other hand, are more digitally engaged as they move beyond the 40 percent digitization threshold. In aerospace and automotive industries, where digitization pressures are lower, only 5 percent of players are making bold moves.

Having a better view of how the market may develop should encourage executives to make decisive moves sooner rather than later. By doing so, they will increase their odds of successfully navigating digitization's perilous break point. Q

[1] Based on an original survey of C-suite executives, with answers from 2,100 incumbent companies in 60 countries: Jacques Bughin, Laura LaBerge, and Anette Mellbye, "The case for digital reinvention," *McKinsey Quarterly*, February 2017, McKinsey.com; also see Jacques Bughin and Nicolas van Zeebroeck, "The right response to digital disruption," *MIT Sloan Management Review*, April 6, 2017, sloanreview.mit.edu.

[2] We asked executives about the nature of their digital strategy, the share of company revenues linked to digitization, and their digital capabilities versus the competition's.

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