What is business transformation?

Business transformations are designed to boost overall performance through increased revenue, lower operating costs, and better customer satisfaction and workforce productivity.
For years now, transformation has been a catchall term for how organizations make the right moves to achieve their full potential. Companies usually aim to deliver healthy financial performance and organizational effectiveness before focusing on higher growth, new strategies, and tech-enabled solutions.

But the pace of change means that waiting to “earn the right to grow” is no longer the best strategic or financial option. Just a few trends tell the story: new digital entrants are disrupting industries, with many capturing more value and significantly higher equity valuations than incumbents; ecosystem-based strategies are gaining ground; companies committed to environmental, social, and governance (ESG) criteria are increasingly standing out; and talent is a bigger priority than ever in the C-suite, as leaders try to ramp up the right capabilities to create value.

In such a dynamic business environment, focusing on new ways of working, new capabilities, and new technologies is the way forward. Yet transformations are not easy to get right. Research by McKinsey has long documented that enterprise-wide transformation is difficult, with less than a third of transformations reaching their goals to improve organizational performance and sustain these improvements over time.

Here’s what years of research have taught us about how to launch a holistic and enduring business transformation.

Who’s involved in a transformation?

The CEO helps a transformation succeed by communicating its significance, modeling the desired changes, building a strong top team, and getting personally involved.

The chief transformation officer (CTO), a C-suite role that is becoming more prominent in many sectors, is the high-level orchestrator of the transformation process. The CTO should be an extension of the CEO, with the mandate and authority to make decisions about personnel, investments, and operations. The CTO may be in charge of hundreds of initiatives, but responsibility for making day-to-day decisions and implementing those initiatives lies with line leaders, transformation managers, and others.

While C-suite attention is crucial, a lot more people are needed to make a transformation work—often 25 percent or more of the workforce. These employees play transformation-specific roles, such as work-stream lead or initiative owner. But what is the minimum level of employee involvement needed to guarantee transformation
success? McKinsey recently looked at data from 60 organizations that are at least two years into their transformations and found that transformations with at least 7 percent of employees owning part of the transformation are twice as likely to deliver better total shareholder returns. While 7 percent may seem like a small number, even at a medium-size organization that can mean hundreds of employees.

**How do transformation leaders achieve their goals?**

The most successful transformations turn ideas into detailed business plans with trackable, time-bound metrics to measure outcomes. Ultimately, these business plans should result in value creation, cost savings, growth opportunities, and other improvements.

Many transformations are enabled by a central transformation office (TO), with the CTO at the helm. The TO defines goals, models new ways of working, and ensures that the overall program and specific work streams stay on track. It also offers a repository for leaders to get help when faced with difficulties and to develop new skills.

Typically, the TO enables results through weekly, action-oriented meetings. Attendees can include a sponsor for each work stream and other key initiative owners, plus representation from finance and the CTO.

Beyond the transformation plan, the TO helps to ensure that the organization changes the way it works over the long term, so that the company doesn’t revert to old ways as transformation initiatives are completed.

**What makes transformations successful?**

According to a McKinsey Global Survey, three core actions are especially predictive of transformations that capture the most value:

- **Using an objective fact base to identify opportunities for improvement.** The more thoroughly an organization uses facts to assess the maximum financial benefit from a transformation, the more confidence leaders will have to pursue ambitious yet realistic targets that reflect the transformation’s full potential.

- **Communicating a compelling reason for why a transformation is necessary.** Simply protecting the bottom line isn’t enough; leaders need to explain why employees should do things differently. If people don’t understand what the transformation means for their daily work, as well as for overall business goals, their mindsets and behavior won’t change and organizational health will suffer. Role modeling, developing talent and skills, and fostering understanding and conviction are ways to make sure people are brought on board and stay there.

- **Matching the company’s best talent to its most crucial initiatives.** This action emphasizes the importance of linking business and talent priorities by creating a clear view of where value is generated in the company, and who in the organization has the ability to deliver that value.

McKinsey research also shows that the execution stage—embedding transformation disciplines into business-as-usual structures, processes, and systems—is key to generating value. Companies that have undergone successful transformations are more likely than others to have made substantial changes to their annual business planning processes and review cycles, from executive-level weekly briefings and monthly or quarterly reviews to individual performance dialogues.

When it comes to widespread results, generous and specific financial incentives are one of the most effective tools to motivate employees. According to McKinsey analysis, companies that implemented financial incentives tied directly to transformation outcomes achieved almost a fivefold increase in total shareholder returns compared with companies without similar programs. In tandem, a well-crafted program of
nonfinancial incentives can create a higher level of energy and excitement across the organization and boost employees’ discretionary efforts.

Finally, speed is of the essence. Companies with top-quartile financial performance typically capture 74 percent of their transformations’ value within the first 12 months. That value can be reinvested in new initiatives, creating a virtuous circle of improvement.

Why do transformations fail?
Several additional behaviors can put a transformation at risk:

— **Declaring victory too early.** In successful transformations, companies typically turn their initial burst of idea generation into an achievable, rigorous plan within a few short months. Unsuccessful transformations don’t sustain that early impact. This can happen for a number of reasons: for example, if budgets don’t stay aligned with objectives, performance and governance discipline can trail off.

— **Not establishing clarity on resources.** Without clear owners and accountability for actions, it’s impossible to embed rapid decision making and to reinforce new mindsets to keep the transformation moving.

— **Failing to refine as they go.** No single action, or group of actions, defines transformation success. However, leaders who invest in tangible changes to business-as-usual structures, processes, and systems; prioritize transformations as the main event; and maintain a long-term mindset can give their organization the best chance at achieving the full potential of its transformation.

According to McKinsey research on successful business transformations, many companies restocked their number of initiatives by as much as 70 percent after the first year. That’s a sure way to maintain momentum for the challenges ahead.

*Learn more about McKinsey’s Transformation Practice, and check out business-transformation-related job opportunities if you’re interested in working at McKinsey.*

**Articles referenced:**

— “Meet the newest member of the consumer C-suite: The chief transformation officer,” December 5, 2022, AD Bhatia, Kevin Carmody, Rebecca Johnson, Emily Rizzi, Jim Scott, and Kristi Weaver

— “You can’t move too fast: A conversation with Andy Penn,” September 6, 2022, Wesley Walden

— “The powerful role financial incentives can play in a transformation,” January 19, 2022, Hugh Bachmann, Robin Ligon, and Dominic Skerritt

— “Losing from day one: Why even successful transformations fall short,” December 7, 2021

— “How many people are really needed in a transformation?,” September 23, 2021, Laura London, Stephanie Madner, and Dominic Skerritt

— “The numbers behind successful transformations,” October 17, 2019, Kevin Laczkowski, Tao Tan, and Matthias Winter

— “The wisdom of transformations: How successful CEOs think about change,” July 23, 2019, Oliver Bladek, James Deighton, Alison Dunn, Tip Huizenga, and Wesley Walden