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Driving Digital Strategy

A Guide to Reimagining Your Business

Framework for Reinventing Your Business

Disruption and transformation get a lot of hype, and for good reason. Digital technologies have had a profound impact on the world, disrupting entire industries while also enabling companies such as Facebook and Amazon to achieve exponential growth. There's no doubt that incumbents have struggled as new and nimble players have emerged with innovative business models. But there's also a more important story to tell: as much as digital has posed a threat to the old guard, and continues to do so, it also presents an endless number of opportunities for companies from traditional industries.

The Weather Company is a case in point. When consumers moved away from TV to mobile phones but did not stay long enough to generate ad revenues, the company execs pivoted and created a service called WeatherFX, which uses data from its app to help retailers predict how the weather will affect consumer purchasing behavior. And other companies are finding success, too. Faced with declining print subscriptions and the loss of revenue from classified ads, the *New York Times* built a

highly successful digital-subscription business with over 2.5 million sub-scribers, and the company is on track to generate $800 million in digital revenue by 2020. Car companies such as Cadillac are experimenting with subscription services, Sephora and other retailers are using apps to enhance the in-store experience, and Goldman Sachs has created an online platform (and asked its competitors to join in as well).

As a business leader, you've no doubt had "digital" on your mind for quite some time, and you've probably started new initiatives and run experiments in an effort to "digitize" your business. Some of these have probably been fruitful. But if you're like the executives I interact with, you're looking to make a more transformative impact. But how? If your company lacks the digital DNA and agility of a startup, how can you take full advantage of the unique opportunities that the digital era provides?

For over ten years, as a professor at Harvard Business School, I've stud-ied digital strategy and have worked with scores of companies on their digital transformations. While doing so, I have seen firsthand what works best and what doesn't, and what I've learned is that the leaders who achieve transformative results go all-in on digital. That is, they don't treat digital strategy as separate from their overall strategy. Instead, they lead with a digital-first mentality and make sure their digital strategy touches *all* aspects of their organizations. Digital transformation requires strengthen-ing the core and building for the future at the same time.

This is what this book, using a broad range of examples, will show how to do. It compiles case studies and best practices from companies who have reinvented their businesses, and provides a framework that will help you create an all-encompassing digital strategy while leading your entire organization through the transformation process.

Where Companies Go Wrong

To mitigate the effects of digital disruption while also exploring new opportunities, companies have typically followed some combination of these three strategies—creating small, independent units or startups within the larger organization; doing a series of digital experiments;

and/or leveraging technology to cut costs and improve efficiency. However, in most cases these initiatives have led to limited success.

Almost every large company launches independent digital units or has outposts in Silicon Valley, with the hope that a handful of young entrepreneurs will spark innovation for the firm. The Spanish telecom giant Telefónica, for example, launched an independent unit, Telefónica Digital, in September 2011. While the parent company had its headquarters in Madrid, the new Digital unit was housed in London with a separate CEO and an independent budget. Like most telecom companies, Telefónica had failed to benefit from the mobile revolution. Instead, new players such as Skype and WhatsApp were beginning to threaten the very core of its business. Telefónica's management hoped that the Digital group would come up with new and innovative ideas for products and services that would provide a future direction for the company.

With an ambitious agenda, the freedom to operate independently, and a large budget, the Telefónica Digital team started coming up with just such ideas. As expected, many of these ideas were quite new for a telecom company at the time. After developing, testing, and piloting them, the Digital group sent the promising ideas to the Madrid headquarters for potential global launch. However, Telefónica faced resistance from country heads who were neither convinced about these ideas nor had the capabilities to implement them. After three years of this experiment, the company shut down its Digital unit in London and moved all activities back to Madrid.

Creating an independent unit is like launching a speedboat to turn around a large ship. Often the speedboat takes off but does little to move the ship.

Next, companies tend to run experiments, which makes a lot of sense given the rapidly changing environment and uncertainty about the future. This journey often begins with a few tactical experiments, typically in marketing departments, where employees are quick to try new social media tools or new mobile platforms. As the excitement around digital spreads throughout the organization, new initiatives start emerging all over the company, leading to a proliferation. In 2012, Kasper Rørsted, CEO of Henkel at the time, realized this when he asked

a team of senior leaders to catalog all of Henkel's digital initiatives. He was shocked to find over 150 separate digital initiatives throughout the company. Many of these started as small experiments designed to solve a specific problem faced by one department or country. Soon new and varied digital initiatives began to pop up all over the company: "hundreds of flowers," as Rørsted described them.[1]

Realizing that this proliferation does not lead to any synergy, companies often start consolidating these disparate initiatives. A team of leaders takes inventory of various digital projects in different functions, brands, business units, and regions, to figure out a way to rationalize and combine them. Often, a governance body is created to approve future digital projects. At this stage, projects that used to be regional might become global, and single-brand initiatives might be scaled up to include multiple brands.

Each stage of the journey may be useful, and even essential, at a certain point in time. Experiments help a company test novel ideas and explore future trends. Proliferation of ideas across business units is a sign of entrepreneurship and enthusiasm. Consolidation is a necessary and effective way to rationalize processes and allocate resources. However, doing experiments without a road map or a sense of direction may give the illusion of success in the short run without making any impact in the long run, and ideas that proliferate without scaling may only waste valuable time and resources. More important, this bottom-up approach tends to be tactical in nature and does not address fundamental strategic issues that the company should be debating.

A third approach is to leverage technology to reduce costs and improve the efficiency of operations. For instance, banks close branches as consumers move to online and mobile banking. Retail stores reduce their real estate footprint and close marginal stores. Processes are digitized and streamlined to minimize overlap and increase efficiency. Many of the internal tasks are redesigned to allow customers to self-serve, thereby reducing labor costs.

Companies should always try to improve efficiency and minimize cost. However, if you rely solely on this approach, you are implicitly assuming that technology will not fundamentally change your

business. Effectively you are assuming that banks, for instance, will still operate as before and that fintech companies won't have a major impact on their business. In many cases this may be a flawed assumption. For example, Alibaba's four-year-old Yu'e Bao fund, set up as a repository for consumers' leftover cash from online spending, has become the world's largest money-market fund, with $165.6 billion under management, overtaking JPMorgan's $150 billion money-market fund.

Essentially, through initiatives like these, managers are using a Band-Aid for a deeper problem. In order to be successful, you can't just create a separate digital unit, or run experiments, or use technology to improve efficiency. Instead, you must make digital strategy an integral part of your overall business strategy. That is, rather than treating digital strategy as a separate exercise, you must embed it into the operations and DNA of your organization, in a way that touches all aspects of your business.

Crafting a Strategic View: A Framework for Reinventing Business

Using numerous examples across a variety of industries, this book provides a framework for reinventing your business that will help you leverage existing assets and pinpoint areas where new capabilities must be developed.

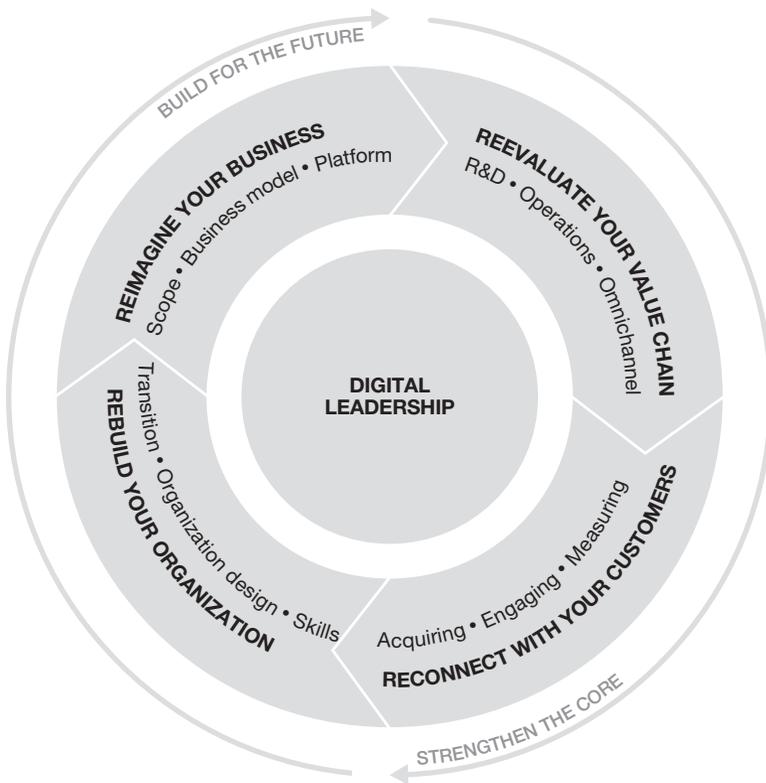The framework consists of four key components:

1. Reimagining your business

2. Reevaluating your value chain

3. Reconnecting with customers

4. Rebuilding your organization

Throughout the book, I'll go into detail about the four parts of this framework. You'll need to face each part head-on. To achieve success,

FIGURE I-1

A framework for digital leadership

you can't tackle one part and not the others. But as you'll see from the wide range of case studies that we'll explore, the options for how you transform your business can be varied, flexible, and open-ended. Knowing that there is no one, magic solution, the book provides instead a systematic approach for digital transformation.

Let's take a brief look at the framework, one part at a time.

Reimagine Your Business

Given the dramatic changes that digital has caused, you'll need to sit back and reflect on the core essence of your business, examining three components: scope, business model, and ecosystem.

When considering scope, you'll need to ask yourself this fundamental question: "What business are we in?" Think about Amazon. It started as an online retailer, but it is no longer just an online retailer. In 2017, Amazon is expected to generate more than $3.5 billion from advertising alone, and its hardware devices, such as Echo, are making significant inroads in homes. Google is moving into autonomous vehicles, and Apple, for years primarily a hardware company, is now investing heavily in original content. What should you be investing in?

Competition in the digital age usually comes laterally, from new players, and redefining the scope of your business is essential to ensuring future success. This requires a careful balance of broadening the scope of your business while staying within your core competencies. Chapter 1 discusses business scope and shows how the rules of competition are changing and what you need to do to stay competitive in the digital age.

Technological changes also require you to rethink your business model: how you create and capture value. For example, when iTunes unbundled the music industry, leading to a significant decline in revenues from recorded music, the industry had to shift its focus to live performances as a major source of income. With the decline in its classified ads, the entire publishing and print-media industry has been forced to consider if its focus on an ad-based model is appropriate for the future. Chapter 2 describes innovation in business models and what your company can learn from these best practices.

As business models change and new competition from different industries starts affecting your business, you may realize that you can't succeed alone. In this case, you may need to evolve into a platform, which will require you to manage an ecosystem of players—both partners and competitors, or "frenemies." Companies have found great success creating platforms, which also led them to redefine how they think about competition.

When Goldman Sachs launched its structured-notes business, SIMON, it shocked the world by inviting its competitors to sell their products on it. This strategy led to Goldman Sachs's becoming the

second-largest issuer of structured notes within a few years. A shift from selling products to creating a platform requires a very different mindset and strategy, as described in chapter 3.

Reevaluate Your Value Chain

Digital technology can significantly improve the efficiency and effectiveness of various parts of your value chain, especially as new models of R&D and innovation have emerged. Companies such as GE, P&G, and Siemens have leveraged open innovation to redefine their R&D process. Chapter 4 describes why and when open innovation works, how you should design open innovation in your organization, and what prevents organizations from being successful with this new approach.

Digital technology has also ushered in a new era of Industry 4.0. Innovations such as digital manufacturing, virtual and augmented reality, 3-D printing, and digital supply chains are improving operational excellence. Chapter 5 describes how firms around the globe are leveraging these new technologies to improve productivity, reduce failure rate, and create competitive advantage.

New entrants often use digital technology to disrupt the existing value chain, especially distribution. In the first wave of the internet, new entrants disintermediated several industries—for example, travel agencies. This process has continued, and now auto dealers and brick-and-mortar stores have come under increasing pressure as manufacturers have started their own e-commerce channels. The challenge for manufacturers is to manage the inherent channel conflict that this situation creates. Every company now has to think about its omnichannel strategy, which creates a synergy between its online and offline channels—a topic discussed in chapter 6.

Reconnect with Your Customers

Digital technology has changed the way consumers search for information and buy products, and technology is enabling firms to collect information about the entire consumer decision journey or path to purchase,

which will open up new ways for you to acquire customers. Long before a consumer buys a car, she searches for information on Google, which provides an opportunity for auto manufacturers to understand her preferences and influence her behavior. Sensors in washing machines will soon allow Whirlpool to understand consumers' usage behavior and even provide valuable consumption data about laundry detergent to P&G. And as consumers increasingly rely on online reviews and friends' advice, you can monitor social media to understand how those friends and reviewers might be converted into brand advocates. Chapter 7 discusses how digital technology has opened new channels for customer acquisition.

Despite all the developments in digital marketing, the click-through rates of ads remain less than 1 percent. Every brand wants to engage consumers, but consumers don't find any compelling reason to engage with, say, a bar of soap, a can of soda, or a bottle of beer. How can you engage consumers in this cluttered environment? Chapter 8 shows that the answer does not lie in technology and data alone but—more generally—in finding new ways to provide unique value to consumers, as done by Tesco in South Korea, Unilever in India, and Mastercard in Singapore.

Digital technology was supposed to make advertising more measurable and accountable. Yet many challenges, such as attribution, remain—making it difficult to measure the effectiveness of ads. How can you measure and optimize marketing spend? Chapter 9 describes new research that points to some useful directions to help companies in this important task.

Rebuild Your Organization

Managing the digital transition in a large organization is a nontrivial task. As you try to strengthen your core business and build for the future at the same time, you'll face the challenge of running two organizations in parallel. As a result, revenues and profits often decline during the transition period before they go back up, which can shake the resolve of even the most confident CEO. Chapter 10 discusses the challenges

in managing the digital transition and highlights how companies like Adobe have successfully navigated this passage.

How do you design an organization for innovation? As I mentioned earlier, creating a separate entrepreneurial group to bring digital innovation into a legacy company is like launching a speedboat to help maneuver a large ship. So instead of launching a speedboat, you must create a "landing dock" where new initiatives, or speedboats, can dock, leverage the power of the mothership, and help change its course over time. We'll cover this in chapter 11.

Data, artificial intelligence, and machine learning are automating tasks and having a significant impact on jobs and the skills and capabilities that companies will need in the future. Technology is also allowing firms to move to a more data-driven and less subjective approach to talent management. New and innovative ways of hiring and managing talent are emerging. Chapter 12 discusses these topics and describes how Knack, a San Francisco–based company, uses mobile games to help its clients recruit talent. Each ten-minute game provides Knack thousands of data points—pertaining to such things as how people process information, how they handle challenges, and how they learn from their mistakes. Knack's innovative approach has won the company ardent fans and influential clients, including AXA, BCG, Nestlé, and Citigroup.

The rest of the book will discuss further the four major areas of digital transformation shown in figure I-1. Each chapter will describe in detail the three topics within each of these areas, highlight best practices, and address some of the questions raised above.