“Digital transformation” has been a hot topic among executives for a decade, often related to the problems, anxieties and fears that get stirred up anytime a new phenomenon arises that requires a radical change to a business’s usual way of working. Lately, however, the conversation has started to shift from resistance to acceptance, as executives see the advantages of digital technologies for relating to customers and competing more effectively in rapidly evolving markets.

Sales and marketing executives are among the leading proponents of this shift. This is no surprise, given that the need for digital transformation is largely being driven by customers and the market, and these executives are well-positioned to pick up on these indicators.

But it is not just a priority for sales and marketing executives. Digital transformation touches everyone: operations, finance, human resources and IT. Yet they need guidance on creating a cohesive digital strategy. When and how to get started? What are the best practices? What can we learn from others, both the successful steps they have taken as well as their missteps along the way?

To answer these questions, we undertook exploratory research with 22 companies from diverse sectors. We combined what C-suite executives from those companies told us about their experiences of digital transformation with
our own review of the current research on the topic. Then, we developed a model, which we presented to half the executives we talked to before as well as hundreds of other managers, in order to incorporate their additional feedback. We call our model the Stairway to Digitalization (see Exhibit 1).

We recognize the muddle that executives sometimes find themselves in with digital transformation, perhaps due to information overload and the rapid rate of change. Our model aims to give order to digital transformation, so executives can identify what stage their company is at, and what factors might be stalling their progress. We have mainly talked to incumbent firms that were not born digital, so our model is especially designed to help them become competitive in a digitally transformed future. However, we think our model can also help digital pure players as they see competitors catching up.

It starts by deeply understanding the market – how it is changing and how this change will impact the firm. Then, senior management must fully commit to the transformation. Lastly, we identify the essential levers necessary for executing the steps, so that the strategic goal of digital transformation might be achieved – resulting in a new business proposition for the firm.

**STEP 1: INTERPRET MARKET FORCES**

Virtually all the C-suite executives we spoke with pointed to changing customer habits as being at the root of digital transformation. Hence, a fixation on customers lies at the epicenter of digital transformation. Consider an industry that has been profoundly affected over the past decade: travel. Customers looking for a place to stay have very different sources of information than they did just a few years ago, such as other customers’ ratings and photos posted on any number of sites such as Booking.com or TripAdvisor. Even after making a reservation, they may keep looking at other hotels and cancel their booking at the last minute if they find a better deal. Or they might rent anything from an apartment to a castle from a private owner on Airbnb. Clearly, the consumer journey has changed a lot.

Worryingly, not all boards and CEOs fully appreciate these changes and where the market might go next. There appears to be a lack of executives and board members with deep knowledge and expertise of the digital world. If the top people in an organization are unable to correctly interpret these changes, they will never be able to start a digital transformation journey.

This is especially important when you consider that it is not just your existing customers that you need to fixate on, but your non-customers, too. It may well be that you are failing to read the signs of digital transformation because your current customer base is not there yet or behaves in an unrepresentative way. You not only need the inside-out market perspective, but you need the outside-in market perspective, too. Non-customers give you additional market information, while your current customer base could be feeding you with self-reinforcing ideas. You want to expand the pie, not just know your own section of the pie really well. It’s Steve Jobs’ maxim that your customers may not be able to tell you what they want because they may not know themselves until they are presented with it.

By all means, start with your customers, but recognize that you need to cast the net wider. Customers’ evolving needs do not happen in a vacuum, but are often shaped by other market actors and the wider environment. Accordingly, managers must be aware of their competitors, collaborators and context.

**COMPETITION.** To set the urgency and pace of digital transformation, the board and the top management team should judge market forces in terms of competitive threats and opportunities, as well as predict the expected speed of market
3 Steps to Market-Driven Digital Transformation

EXHIBIT 1
The Stairway to Digitalization
THIS STEP-BY-STEP MODEL GIVES AN ORDERED STRUCTURE TO DIGITAL TRANSFORMATION.

1. Interpret Market Forces
2. Ensure Digital Commitment
3. Execute at the Right Speed

change. Exhibit 2 on page 19 is a familiar matrix for doing this exercise. Some firms will see more threats than opportunities and also expect change to be fast: in these cases, they should act fast and leave very little room for failure. Others may be just as concerned, but the changes, for them, will be slower: banking could be an example. Some companies will be optimistic about the changes ahead. For those in this category who expect change to be slow, they can take more time to plan their next move. Others, however, will need to act fast to prevent competitors from benefiting from the same process of digitalization and taking market share away from them, as is happening among Uber, Lyft and Cabify.

Being able to grasp the threats and opportunities is important, but the speed of change is critical, because if the changes are going to accelerate, you had better start running fast.

As mentioned earlier, the travel sector has already been significantly disintermediated by metasearch engines, online travel agencies and hotel room resellers, so incumbents in that sector have a pretty good idea of where the changes are occurring and at what speed. In other sectors, the changes are relatively slow, making it harder to anticipate market trends. Universities, for example, could be affected by sites like edX or Coursera, but compared with what’s happening in the travel sector, the digitalization of education is still in its infancy. And in other industries, like meat, managers do not yet fully understand the greater efficiencies afforded by digitalization to their supply chains. The real question for them is when will these changes start to speed up?

In our opinion, this is where many companies stumble: they don’t adequately consider the speed of change. Because digitalization has not wreaked havoc on their business as much as it has on another, they lull themselves into a false sense of security, believing that change will never be as drastic for them. But no one is immune, not even those sectors that have remained comparatively stable until now.

Senior executives should be closely monitoring the market in which they do business. The sectors most affected by digitalization are nowhere near reaching a stable phase yet, and in
3 Steps to Market-Driven Digital Transformation

other sectors the process of digitalization is only just beginning. No executive should be complacent, thinking that his or her business model will escape unscathed. Failing to position your firm in the opportunities/threats vs. speed-of-change matrix of Exhibit 2 could be lethal.

COLLABORATORS. When a market is going through a transition, new collaborators emerge. Going back to the travel example, you could argue that sites like Booking.com are only digital versions of traditional agencies. However, those online travel agencies change the rules of the game and also shift the balance of power in the channel. They are much more powerful than traditional agencies, because they capture a significantly higher percentage of customers and, together with metasearch engines like TripAdvisor, add transparency to the market. As such, consumers have more information, which usually results in more price competition, and intermediaries gain more market power.

Many firms will recognize similar dynamics in their own industry, as they find themselves having to depend on companies that are playing much bigger roles in new and unexpected ways. For example, a boiler manufacturer probably never thought it would see Google disrupt its market. Some years ago, Google bought Nest, a manufacturer of digital thermostats. If enough household boilers are connected to these thermostats, then Google will have access to a goldmine of customer information, which it could sell not only to boiler manufacturers but to installers and energy companies, among others. While this might provide a new advertising channel to acquire customers, it might also be an expensive one for boiler manufacturers. This is an expression of the Internet of Things, and as this phenomenon takes hold, manufacturers of any device susceptible to being connected to the internet will invariably find themselves interacting with new market collaborators and, by extension, new sources of competition.

The same goes for many household brands. Social media sites and online influencers are increasingly strategic partners for building brand awareness and liking. Companies need to learn how to manage these collaborators.

Consider Vodafone Spain. To capture the youth market, it launched Vodafone Yu, which it promotes via its own radio program and a TV program on Comedy Central featuring popular YouTubers. This shows the range of partners extending, new sources of competition.

CONTEXT. The context (economic, cultural, political, legal, etc.) in which a firm operates is the final piece to understand the market forces of change. For example, the protections afforded to taxi drivers in cities and countries around the world have greatly conditioned the development of Uber and Cabify, and in some cases, slowed their progress. Banking is another highly regulated industry that has conditioned the pace at which fintechs have been able to grow.

If your business operates in an industry where strict protections may keep digital disruptors from growing too fast, then you should use that competitive advantage to move up the Stairway, as you closely monitor the evolution of the market context. Remember, markets can suddenly pivot, so you also have to anticipate the future. To this end, executives should regularly engage in scenario planning.

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STEP 2: ENSURE DIGITAL COMMITMENT

Understanding market forces is a necessary first condition for digital transformation to happen – but it is not enough. The next important step
is for the executive committee and board of directors to be unequivocally committed to the change. To achieve this “digital commitment,” we find the following factors help.

**LEADERSHIP.** CEOs, with the support of their boards of directors, must be capable of communicating their digital vision to their companies. In organizations where digitalization runs the very real risk of cannibalizing existing revenues, this may be a hard sell. For other organizations where the digitalization trend is not as pronounced, leaders will have to convince others of the need for change.

One executive from a family-owned business told us, “The members of my board largely feel that the digital world will not impact our business. Why all this need to go digital when we sell industrial furnaces?” Yet this same executive also felt that furnaces were digitizable, perhaps by connecting them to the cloud to measure their efficiency, and then starting to sell solutions instead of products.

A good leader who understands market trends and can imagine the future will be able to set the direction and speed of transformation.

**STRATEGY.** There is no universal digital strategy, but the digital dimension will inevitably affect any strategy.

The CEO of a major seed producer explained how farmers were using new technologies to control their crops. They would get information about new varieties of seeds online, watch tutorials on YouTube, and monitor weather forecasts and control irrigation using their smartphones.

Although these may seem modest changes, they have led the company to change its distribution strategy, increasingly connecting directly with end consumers rather than relying entirely on an extensive network of distributors. Even “small” shifts such as these pose significant strategic risks, illustrating how meeting the needs and demands of customers will involve some degree of redesigning existing strategies.

**INNOVATION MINDSET.** Digital transformation will involve innovation in products and services, pricing models, distribution channels, communication strategies, processes and/or the supply chain. In sectors where stability is the norm, innovating fast will be especially hard. Does the senior management have the right mindset for digital innovation?

There has been much research done on “design thinking,” dating back at least 40 years but given fresh impetus in recent years by companies like IDEO. Essentially, it is a form of creative problem-solving that, instead of using observable facts to postulate a solution, starts with needs and works backwards in an iterative process to arrive at various possible solutions. This is especially relevant when it comes to digital transformation, where many possible paths need to be explored simultaneously, as any one of them could suddenly take off.

Recognizing the need for speed, responsiveness, adaptability and delivering on multiple fronts at once, researchers also talk of “ambidexterity” or “multimodal” approaches – in other words, being capable of managing legacy systems while at the same time innovating and being ready to pivot or scale up at a moment’s notice. In some cases, companies set up two units to innovate at two speeds: one to execute for today, while the other works in parallel to experiment and transition to digital for tomorrow.

IESE colleagues Evgeny Káganer, Javier Zamora and Sandra Sieber have written extensively about this “digital mindset,” calling on organizations to cultivate this vital ability to hold two seemingly paradoxical or contradictory
Many companies have executives who are good at designing a roadmap to digital transformation, but then invest timidly. Transformation cannot happen if the emergency brake is left on.

realities together at the same time. Only by managing this tension will companies be successful at digital transformation.

**INVESTMENT.** Leadership, strategy and innovation are not sustainable without monetary investment. Many companies have executives who are capable of understanding market trends and are good at designing a roadmap to digital transformation, but then invest timidly, perhaps because their boards are too cautious and reactive. Transformation cannot happen if the emergency brake is left on.

One executive from a large multinational told us that, in his experience, leadership, strategy and innovation were the hard ones, and that getting investment was the "easy" part. However, for other firms, particularly small and medium-sized enterprises, the necessary investment cannot be justified so easily. Moreover, how can a mid-sized hotel chain compete in capturing leads for its locations against a company like The Priceline Group, which invests a disproportionally higher amount in Search Engine Marketing (SEM), Search Engine Optimization (SEO) and user experiences for its websites?

Sometimes the gap between the desired and available funds is just too big. Even so, companies need to allocate appropriate investment to proceed. This means articulating a long-term strategy that addresses the main stumbling blocks to digital engagement, such as the potential cannibalization of the core business.

**CULTURE & TALENT.** Adapting to the appropriate pace of transformation can only happen if there is a cultural change and the right talent is in place. What does this take? It involves more than just breaking down the silos that predominate in many organizations, or hiring in a few technology experts. It’s about getting key people in the organization to become agents of change.

For this to happen, people must work together well as a team. They must resist inertia and complacency. There must be a constant desire to innovate — to experiment and adapt to new realities, as the business is exposed to an exponential series of changes. People must be allowed to make mistakes — and they must be humble enough to admit them. And when people fall short, they must be quick to make amends.

Getting the right talent with the digital skills and mindset is proving elusive for many companies. Numerous studies in recent years have testified to the scarcity of digital talent. It’s not just that genuine digital talent is hard to find but that many companies are at risk of losing what talent they have because they are not developing their people adequately.

A 2016 study by MIT Sloan found that over half of employees at companies in the early stages of digital transformation said they were planning to leave their organizations in the next three years, while 1 in 5 said they would be gone within the year, including around a third of senior vice presidents, vice presidents and directors, owing to a lack of digital development opportunities. It doesn’t have to be so, if companies would make digital talent development a priority.

A McKinsey report suggests practical ways that companies can raise their digital talent quotient. A lot of talent can be nurtured by focusing on competency development inside the firm, it says, rather than always recruiting technical specialists from outside. Particularly during the early stages of digital transformation, basic
3 Steps to Market-Driven Digital Transformation

digital competency may matter more than deep technical knowledge. Companies also need to get creative with training. McKinsey cites an initiative whereby Procter & Gamble and Google swapped employees so they could learn from each other about SEO and SEM.

**Processes.** A meat company may not be able to digitize its cows, but it can take numerous processes digital. It can roll out a good customer relationship management (CRM) solution for its sales force, or use GPS devices in its trucks, and leverage that data to establish new delivery routes. Rather than leaving it up to an area manager to decide which customers to serve first, an algorithm could be created to determine a logical route using information such as traffic, the customer’s historical margin and preferred visiting hours. A growing number of companies are using IBM’s artificial intelligence application, Watson, to crunch data and even substitute for many human decisions, helping to increase the efficiency of their existing processes.

**Digital Assets.** Though building digital assets has become an imperative, we should broaden the definition beyond the marketer’s understanding. In our view, a digital asset could be anything from a website, to an app, to a proprietary algorithm to optimize your SEM, to a facial recognition system, to a GPS device that tells you where your drivers are.

But remember: digital assets are not an end in themselves. They are tools to change processes and improve customer relationships. Some are customer-facing (websites or apps). Others are not directly observable (algorithms). But they are all important.

Many companies fail to grasp this basic point. For example, some retailers spend millions to establish a single physical store – a flagship in a specific geographical area – but then skimp on their website, perhaps their most important store.

**Data & Analytics.** Another key issue is that many companies attempting to brave the unknown world of big data are still having trouble mastering small data. Granted, there are a number of cloud-based or Software as a Service (SaaS) tools available that have helped to simplify the process of analyzing data. However, as the amount of data grows exponentially, some sectors – including banking, supermarkets and telecommunications – face endless possibilities. This makes it all the more important that companies find talent at the analytical and business level who know how to live with this abundance of information and who are able to integrate its use into the corporate strategy.

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**Exhibit 3**

**Watch Your Step!**

**Avoid These Common Mistakes at Each Step of the Digital Transformation Journey.**

**Step 1: Interpret Market Forces**
- Lack of customer orientation
- Superficial information about market trends
- Failure to account for the complexity and speed of the changes
- Wrong management profiles

**Step 2: Ensure Digital Commitment**
- Lack of vision and digital mindset
- Lack of resources
- Short-term orientation: only working for today rather than planning for tomorrow; only working at one speed instead of two
- Fear of cannibalizing the existing business
- C-suite executives having different visions

**Step 3: Execute at the Right Speed**
- Too much organizational bureaucracy
- Slow decision-making processes
- Reactive culture
- Lack of digital talent and talent flight risk, owing to a lack of digital development
- Slow-moving IT department and overly complex IT systems
Problems arise when IT and business speak two different languages. It is impossible to achieve digitalization if there is no alignment between IT and those responsible for strategic business objectives.

Once you have undertaken Steps 1, 2 and 3, you are ready to combine them to form the final shape, which is your New Business Proposition. Then, you need to keep monitoring progress, reviewing market opportunities/threats and the speed of change in a continuous feedback loop that yields fresh insights. Based on preliminary findings from our research and conversations with executives thus far, we believe the Stairway to Digitalization provides an extremely useful framework to help you get started on the journey to transform and adapt your organization to the new era.

Time to Step Up

The path to digital transformation is rife with obstacles (see Exhibit 3 on page 21). Admittedly, it is harder for incumbents than those born digital. No matter how strong its digital commitment, a banking institution will have bureaucratic hurdles and complex legacy systems to contend with, which an agile digital startup won’t. New digital pure players can just skip up the steps of digital commitment and mindset.

That said, digital newcomers will stumble on certain steps: the questionable legal contexts in which some operate, their more relaxed views on data-sharing and privacy, their lack of established customer bases and brands, and their smaller reserves of money for future, long-term investment mean that their market domination is not guaranteed.

TO KNOW MORE


