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Digital strategy

Paul Willmott

Digitization is fundamentally altering the nature of competition. McKinsey's Paul Willmott explains how digital winners think and what companies can do to compete.

Incumbent companies face critical decisions when it comes to addressing digitization. In this video interview, McKinsey director Paul Willmott argues the first decision is fundamental: whether a company is even in the right industry. That's because digitization is blurring the lines between sectors, placing fresh demands on both leadership and organizational strategy. This interview was conducted by McKinsey's Bill McIntosh, and an edited transcript of Willmott's remarks follows.

Companies need to make several key decisions around how they're going to address digital. The first one is "are they in the right businesses to start with?"

The future is now

It's true that companies have been using technology for many decades. But a few things have changed. First of all, customer expectations are very, very different now. We know that around 80 percent of purchases are researched online before a customer goes into a store. Indeed, many customers now prefer to complete the purchase online. Even in groceries, over 10 percent of customers in the UK now will shop online and actually make the purchase.¹ In banking—in this country, in the UK—it's over 30 percent.

The second thing that's changed is that the cost of delivering high-end IT solutions is reducing all the time. Historically, it would have been very expensive, and a lengthy process, to deliver a highly functional technology solution that customers would want to use. That's no longer the case—it can sometimes be done now in just weeks or months.

Digital is fundamentally shifting the competitive landscape in many sectors. It allows new entrants to come from unexpected places. We're seeing banks get into the travel business in some countries. We're seeing travel agents get into the insurance business. We're seeing retailers go into the media business. So your competitor set is not what it used to be.

¹ For more, see Nicolò Galante, Enrique García López, and Sarah Monroe, "The future of online grocery in Europe," April 2013, on mckinsey.com.

One thing that digital allows is what I call “plug and play dynamics”—meaning that companies can attack specific areas of the value chain rather than having to own the whole thing. This is because digital allows different services to be stitched together more quickly and cheaply.

How digital winners think

Digital winners are thinking broadly about whom to collaborate with. In some cases, that may include collaborating with firms that would have been considered competitors historically—or, at the very least, collaborating with firms that can share data with you.

Digital winners are also creating the right scale of investment in their IT infrastructure. It's very hard to keep up with the pace of evolution in the digital world unless you have a flexible IT infrastructure and one that can plug and play products and services from other places. Some renovation is required in many companies.

Making key decisions

A key decision around digital is whether to attack or defend. For many incumbents who are in a high-margin business, it can be hard to imagine the need to set up a low-cost, innovative proposition, to target your customers, because it can destroy value in the short term. On the other hand, defending for too long—if there are aggressive attackers in the market—can lead to a long-term problem if those attackers are sufficiently more attractive to customers or have a lower cost base. So companies need to think carefully about the right balance of attack and defend.

It's important early on to understand what, really, is the value from digital. There's an awful lot of hype around digital, from many sources. One way of cutting through that is to understand the potential upside and downside to the P&L in the medium term.

In many industries, there are opportunities that come from new channels or low-cost entry into new markets. But there are also threats that come from improved price transparency that leads to margin compression. Understanding the relative weight of those opportunities and threats is a good way of understanding the amount of investment that digital warrants and the speed at which action is needed.

Incumbents have many strengths that they can play on as they defend against digital attackers. They have, for example, a customer base. They have a brand. And they have data. The trick, however, is to make sure that all of those assets are leveraged and used equally well in the digital world. For example, making sure that the data they *do* have is used in an effective way for insight and for your presentation of the right marketing and offers in the digital space.

Deciding who drives

Many CEOs are choosing to lead the digital transformation themselves. That's particularly true in the industries that are being heavily disrupted. Because, in that case, it's a do-or-die situation. The other reason why CEOs often need to be personally involved is because digital impacts many of the different functions at an organization. It's very hard to delegate it to one person because, in fact, it impacts most of the organization. The challenge for CEOs is carving out enough time. On the whole, they'll have very full agendas and digital is just another thing to be added to a long list, typically.

One solution is for a CEO to delegate the digital agenda to a chief digital officer. That can be very effective. But it has its challenges. Specifically, it can be difficult for a chief digital officer to have enough influence to make the changes they need across the whole organization.

To give an example: a bank wanting to create a seamless customer experience needs to change marketing, needs to make changes to the products, needs to make changes to distribution, and needs to make changes to operations and to technology. It can be hard for a chief digital officer to have the mandate and the impact across all of those functions.

In some sectors, it's easier for the CEO to delegate the digital agenda. For example, in a consumer goods company, often the main impact of digital is in the marketing function. Therefore it can make sense for the chief marketing officer to take control of the digital agenda. □

Paul Willmott is a director in McKinsey's London office. This interview was conducted by McKinsey's **Bill McIntosh**, who is also based in the London office.

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