A TALE OF TWO MISSIONS:
FROM IT MODERNIZATION TO
BUSINESS TRANSFORMATION

Executive Summary
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In recent years, the term 'digital transformation' (DT) has pervaded the business press, becoming one of those buzzwords that's almost impossible to avoid. But while it's easy to mock and dismiss the catchy phrases of the day, their rise and fall is usually telling us something about developments in the real-world marketplace. The question is: what?

For more than a decade, large organizations have been migrating to cloud computing, Software-as-a-Service (SaaS) and other internet-based services. But the global technology community now anticipates a much more powerful wave of change based upon various combinations of smart products, machine learning, industry-specific business platforms, algorithmic processes, robotics, self-service, data-driven operations and new forms of value creation. Taken together, these capabilities provide a vision for transformed, 21st century organizations that look much more like today's digital giants than the traditional global firm. It's hard to over-estimate the potential of these changes.

To help our clients better understand where we are in the digital transformation journey, we have conducted in-depth, face-to-face interviews with leaders in some 30 large organizations. We have also carefully examined the vast quantity of external digital transformation research. However, this latter effort proved to be mostly a disappointing task; it soon became clear that the marketplace has struggled to assess and write about DT in a consistent and useful way, and this has only added to the overall industry confusion. In our report, we hope to clarify the myths and realities, and provide a solid steer through today's two main DT missions – near-term IT modernization and long-term business transformation.

**What do we mean by digital transformation?**

It quickly became clear during our interviews that the term 'digital transformation' is unusually divisive. For some, it's a useful way to describe their major change initiatives. Yet with quite a few others, it's seen as either vendor-driven hype that distracts them from the real challenges they face, or even as a potentially demeaning way to portray how things are currently done. Indeed, we came across more than one instance of the term being essentially banned, as well as the purposeful removal of the word 'digital' from many job titles.

While there is surely a lot of puffery in the market today (when hasn't there been?), we disagree with those who largely dismiss the overall DT concept. Virtually every traditional large organization we work with is wondering whether it will eventually need to operate much more like today's dot.com leaders, and there is great interest in what others are doing, as well as a real fear of missing out.

Similarly, some interviewees said they prefer to drop the 'digital' and just use the term 'transformation', but this can be misleading. Digital transformation is just a subset of transformation overall – in that there are undoubtedly non-digital forms of transformation as well. Consider how genetics is transforming pharmaceuticals, and fracking the fossil fuel industry. Like it or not, to talk specifically about change driven by information technology, the word 'digital' – or an equivalent – is very much necessary, simply for clarity.

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To provide more tangible, working definitions, LEF segments things that are often called ‘digital transformation’ into the three broad categories shown in the figure above:

- **IT modernization** is far and away the most prominent form of change observed, as just about every large organization wants to build a more agile and efficient digital foundation or core – and in its more advanced forms a full-blown digital twin. This usually involves moving to various cloud and SaaS capabilities and developing the skills and culture to use them effectively. Much of this modernization is managed by traditional IT, and it often involves a complex and mission-critical process of detailed change management. If one sees significant operational modernization as a form of transformation (as many people understandably do), the DT market is very large indeed. It’s what most organizations are actually doing today, typically with steady success. However, some organizations are considerably farther down this road than others.

- **Business transformation (BT)** is considerably less common, as it occurs when an incumbent organization successfully makes a major shift in strategy, business model, value proposition, organization or culture. BT is how existing firms successfully adapt to major marketplace shifts. Today, this typically involves advanced pursuits such as software-defined operations, automated/learning business processes, new forms of data monetization, and a strong, digital-first customer experience. If you only use this narrower definition, the DT market is highly strategic, but considerably smaller in terms of customer spending. But as this type of fundamental business transformation is at the heart of making 20th century firms operate more like today’s 21st century leaders, BT is the primary focus of our report.

- **Industry disruption** is clearly another major buzzword of our time, and rightfully so, as the displacement of incumbent industry leaders by new technology-led rivals has already transformed some industry sectors and is a looming possibility in many others. While we typically think of disruption as being led by start-ups with new business models, it can also come from sources such as China, various political/economic shocks and/or natural disasters. Disruption is where the biggest strategic shifts periodically occur, and therefore it is almost always of interest to senior executives. In our view, industry disruption is essentially the opposite of business transformation. In the former, the new players win; in the latter, the incumbents prevail.

Virtually everyone we talked to mentioned how difficult both IT modernization and, especially, business transformation can be, with the list in the figure on the next page summarizing the ten most common reasons. This helps us understand why, although most companies can easily imagine a highly transformed digital future, day-to-day priorities, politics and norms tend to get in the way. Organizational silos, excessive duplication and the logjams of matrix management were also cited as major barriers to change. Taken together, they help us understand why while it is easy to launch internal digital initiatives and incubators, making change stick at scale often proves elusive.

And of course, there is also the cost. As modern businesses are understandably focused on their results this quarter or this year, it can be very hard to build consensus around the need for sustained digital investment, where the payoffs are often uncertain or perhaps years in the future, when the current executives may not even be around.

Enterprise IT faces similar financial constraints. Most IT organizations see themselves as under tremendous budget and workload pressures, and thus find it difficult to pursue major agendas that don’t have a relatively quick payoff. Even if the money is there, the people and skills often aren’t, which is why so much of the heavy lifting of IT modernization is now assigned to technology partners/suppliers.

**So how are companies overcoming these challenges?**

Clearly, it is very easy to identify the barriers and challenges, the obvious question is how to overcome them. Below are some of the main ways in which firms are cutting through today’s DT inertia:

- Arguably, the most immediate path is leveraging a *burning platform* – a situation grave enough that major changes are clearly required. Think about how in a world of internet, IoT, mobile and social technologies, Microsoft could no longer successfully build itself entirely around Windows.

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Agriculture is a good example of an industry that might soon reach the burning platform stage due to growing societal concerns about industrial farming, fertilizers, antibiotics, waste, pollution, water usage, safety, climate change, labour availability, animal treatment and other factors. Brutal competition from China/Asia is also forcing many firms to seek new value propositions.

• However, not every industry has a burning platform. Indeed, most of the companies investing heavily in DT are actually thriving, as they can afford it, and want to be seen as market leaders. The John Deere, Bayer, professional services and oil and gas examples in the full report all fall into this category. While one often hears that the companies that are most advanced in their IT usage are also the most successful, it’s very difficult – arguably impossible – to separate correlation from causation. All we know for sure is that successful firms have more money to invest in various transformation initiatives.

• For companies where money is tight (i.e. most), perhaps the simplest technique we’ve seen is negotiating a bargain. We know several CIOs who have proposed to management that they can cut current IT operational costs, but they would like to do it with the proviso that all or some of these savings be used in more strategic areas. When successful, this approach can generate broad-based buy-in and prepare the firm for the future, while motivating and developing key digital leaders and staff.

There are many reasons why digital transformation is hard. Which suppliers/partners can help?

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• A more strategy-driven approach is for companies to intentionally embrace markets that are more inherently digital. A good example is Philips, which has shed businesses such as lighting, and focused on the more intrinsically digital world of healthcare. While this approach isn’t practical for every firm, it reinforces the view that some businesses are fundamentally much more digital than others. Similarly, DBS Group (formerly Digital Bank of Singapore) is committed to being a digital banking leader because senior management deeply believes that it needs to operate much more like Amazon and Alibaba than a traditional financial institution.

• Last, but not least, strategic alliances or acquisitions can also be an effective way to jumpstart DT efforts beyond what internal start-ups and incubators might do. Consider the way the US supermarket chain Kroger has looked to Ocado, the UK grocery delivery company – and technology platform innovator – for order fulfilment. Ocado also handles home deliveries for the UK supermarket firm Morrisons.

However, even when these diverse strategies and approaches are used effectively, business transformation remains a long-term journey that will run far into the 2020s. We have seen no real shortcuts.
Conclusion and action plan

Successful digital transformation requires a considerable amount of faith, confidence and perseverance at the highest levels of the organization. While some industry and technology forecasters have better track records than others, no one really knows how societal tastes and pressures will change, how quickly machine intelligence will advance, what new platforms will emerge, how China and India will alter the competitive playing field, or how different the organizations of the future will ultimately be. No amount of data can answer these questions.

What we do know is that information technology has already transformed or disrupted huge parts of the global economy. We also know that the current wave of automation and intelligence technologies holds at least as much – and we think even more – potential than anything we have seen thus far. While there are many uncertainties regarding timing, it’s hard to bet against these developments over the long course of the 2020s. Today’s digital business leaders understand this intuitively.

It is this tension between highly significant expected changes and highly uncertain timing that shapes the digital transformation mission today. As shown in this summary and discussed throughout the full report, we recommend an integrated strategic, technical, organizational, leadership and cultural DT agenda, pursued in two main phases:

First, companies need to modernize their core IT foundations so that they are prepared to respond to market changes whenever they come, while sharpening their sense-making and anticipatory skills so they can gauge the rate of change better than their rivals.

But, more fundamentally, they need to believe that over the next decade, digital technologies are likely to reshape just about every industry, as data, intelligence, connectivity and automation are brought to bear on virtually every business and human activity. And once an organization embraces this view, the phrase ‘digital transformation’ is no longer just a glitzy buzzword; it’s the term we use to describe the process through which 21st century global market leadership will eventually emerge.

A ten-step DT action plan

1. Establish visible C-level advocacy, commitment & participation
2. Communicate a clear & specific mission, need, purpose & funding model
3. Acknowledge & leverage any burning platforms
4. Assure a modern technical, & especially a modern data, foundation
5. Improve company sense-making & situational awareness
6. Recognize that transformation will likely cut across existing organizational silos
7. Continually develop 21st century executives, leaders & employees
8. Embrace a strategic set of ecosystem partners & suppliers
9. Keep close track of actual & expected costs and benefits
10. Expect a long journey that will change course often & in mid-flight

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