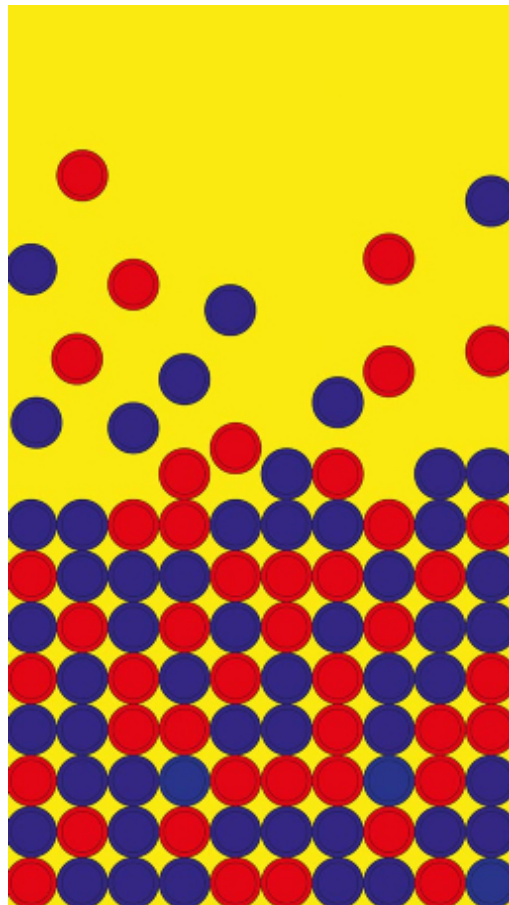


STRATEGY

6 Digital Strategies, and Why Some Work Better than Others

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Digital technology has been roiling markets and disrupting companies for more than two decades, but despite that lengthy history, incumbents are still struggling to enact and deliver on digital transformations.

The first challenge is disruption; digitization is enabling new, disruptive models that aggressively compete with legacy models, putting material pressure on incumbents' revenue and profit growth. As incumbents fight back with their own digital strategies, our research shows that they often trigger a second wave of competition, closer to the notion of Schumpeterian imitation where incumbents start themselves to innovate, sometimes aggressively, against the threat of entrants slashing yet more revenue and profit growth. [We estimate](#) that on average, both waves of digital competition has taken out half of the annual revenue growth and one third of the growth in earnings from incumbents that have failed to respond to digital.

The second challenge is that, even when companies do launch transformations in response to competition, the results are often underwhelming. Based on our recent [worldwide survey](#) of 2,000 incumbent companies across all major industries and countries, we estimate that the average return on incumbent digital initiatives is below 10% — barely above the cost of capital. Besides the average, however, we also witness in each sector a large spread among firms in terms of their ability to sustain growth and generate a return from their digital investments. The top-performing decile of companies achieves revenue growth that is eight percentage points higher than the industry average and a digital ROI that is 10 times that of the bottom decile companies.

To understand what these outperformers do differently, we dug deeper into the data and found that the degree to which they reshuffle their activity portfolio (eg, by selling some activities, buying new ones, or materially reallocating investments among remaining business lines) as well as to which they adapt position in their industry value chain mattered enormously, both in achieving higher digital ROI and reversing the digital curse of low growth.

We clustered companies in two ways. First, based on the level of boldness of their corporate strategy, as measured by the degree of changes above, and extended to two measures of firm commitment to radical change, eg how they are doing those changes at the expense of cannibalizing their current revenue and profit pools and how they are willing invest in digital technology. The higher the share of cannibalization and the higher the investment devoted in comparison to competitors/peers, the bolder the strategy; using our classification, we found four distinct clusters. In particular 13% of companies are part of the most offensive cluster (which we call “big and bold”), which is composed of companies which are more radically adapting portfolio and investing significantly more than peers, with high rate of current revenue cannibalization. Further, a clear pattern is emerging: The bolder the digital strategy, the more likely the company is to have a successful digital transformation. In our dataset, bold corporate strategies were associated with significantly superior performance on all counts: revenue growth, profitability growth, and return on digital investment.

We then classified companies based on the *digital strategy* they were pursuing. To do so, we outlined six digital strategies. The first three are primarily offensive, targeting new demand, new supply or new business models. The second three are defensive in nature, since they are aimed at improving what the firm already does.

The six types of digital strategy

Platform play: One third of firms have engaged to some degree in platform strategies, in an attempt to redefine their industry’s value chain so customers and suppliers can interact more directly and benefit from network effects. Platforms have the power to radically alter the way value is distributed in a value chain. Accor, which is opening its online booking platform to independent hotels offers a good case.

New marginal supply: A smaller fraction of [incumbent firms](#) (13%) were using digital technology to tap into previously inaccessible sources of supply at a marginal cost, often, but not always, in

combination with a platform play. Examples include the Swedish retailers H&M and Ikea, both of which are offering a [online reseller options for their own customers](#), allowing them to sell used, branded products to one another.

Digitally-enabled products and services: Other companies, some 55%, were using digital technology to create new products or services with digital features, typically to serve new demand. One example is P&G's Oral-B toothbrush with Bluetooth-enabled digital guidance.

Rebundling and customizing: Another 60% of companies are using digital technology to rebundle their products or services to better serve their existing customers. The paywall for news content erected by the New York Times where people can personalize reading lists and organize the content they read is a good example.

Digital distribution channels: Many firms – almost 60% – invest in digital distribution channels, in an attempt to make it easier for customers to access their products or services.

Cost efficiency: Almost half of companies we looked at were using digital to improve their cost efficiency, typically through automation or cost scaling. In an age where operational excellence is the norm, this strategy looks like it's aimed at survival rather than creating a source of comparative advantage.

We found that successful companies, especially those with a bold corporate strategy, were considerably more likely to employ one of the three offensive digital strategies. Successful digital transformations are significantly less focused on cost efficiency and more focused on new products or new customers.

For companies committed to transforming and adapting, the key is to make sure that their strategy really *is* transformational and not just a bundle of cost-cutting measures. Our data shows that, while digital attackers often enter markets with a platform-based business model, only a handful of incumbents have done so. In effect, incumbents are losing because they're playing defense. For companies looking to successfully ward off digital disruption, they have to play offense.

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