Chapter 1

BUSINESS TRANSFORMATION CHANGE

The only way you survive is you continuously transform into something else. It's this idea of continuous transformation that makes you an innovation company.
—Ginni Rometty

This chapter characterizes the change in a business transformation. It begins by examining the reasons businesses undertake transformations and describing the types of changes initiated during a transformation. It then looks at the resulting change impacts and introduces a way to measure the degree of change impact in a transformation. This method of characterization allows a company to predict the magnitude of change impact for its transformation.

The Business Transformation Change Cycle

Business transformations are complex, large-scale changes to your company's business capabilities and behaviors—to bring about significant improvement in performance. You can find many variations of this definition in books, articles, and websites, but they all share the notion of change. A significant part of the company must change during a transformation; otherwise, it's hardly worth undertaking. Some of the changes are obvious, and others are not so obvious. It is important to understand both types.

Business change can be characterized as a continuous cycle that never ends. One way to represent this cycle is shown in figure 1 (below).

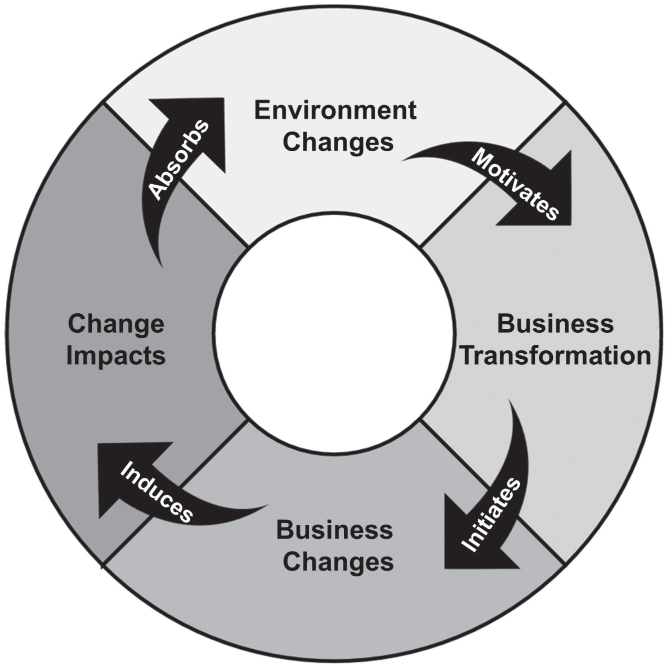

Figure 1. The Business Change Cycle

The business change cycle is interpreted from the perspective of your company. Beginning at the top, changes naturally occur in your business environment. These environment changes serve to motivate your business to undertake a transformation. A business transformation is under your company's control but is a response to something that has occurred in your business environment.

Your business transformation will then initiate one or more changes in your business. Business changes are the changes you elect to make as part of your transformation. They are the most visible and easily recognized changes. The business changes serve as the transformation's focal point.

The transformation becomes more complicated as business changes induce impacts on your business. The change impacts are not always visible or obvious. They require effort to identify and effort to determine their influence on your company. Quite often, they are ignored completely—at the detriment of the business transformation.

Finally, your business must absorb the impacts of these changes. Absorbing change impacts means your business has internalized them, making them part of your operation. This completes the cycle and positions your business to experience new changes in the environment.

The business change cycle is complex enough as a single sequence of change. However, multiple cycles can occur simultaneously. Before your business has fully absorbed the changes and impacts of your transformation, the environment can change again. This is indeed the case in our rapidly changing world.

There is value in characterizing change using the business change cycle. The relationships within the cycle allow a business to understand the scope of change and even predict the magnitude of change impact. This is a powerful tool for transformation readiness.

Why Most Business Transformations Fail

The rate of success (or failure) in business transformations has been studied for more than a decade. Highlights of these studies are covered in chapter 2. While many factors contribute to the poor success rate, a single theme is woven throughout the failures: the breadth and depth of change in a business transformation is unwieldy. The argument made in this book is that most businesses are simply not ready for this level of change. Fortunately, all is not lost as there are methods for assessing whether you are ready, and if not, what you can do to be ready. As stated in the opening, much of this book elaborates on these methods. For the time being consider the following basic readiness deficiencies.

- Willingness: Business transformations are not the purpose of a company. A company's purpose is to profitably service its customers. Senior business leaders would like to get this change completed as quickly as possible and get back to running their businesses.
- Ability: Business transformations are not something most companies do. Consequently, they do not have the right skills in sufficient quantity to address the change.

These deficiencies result in a gross underestimation of the change associated with a business transformation and dooms the transformation before it is started. If you're going to expend the resources to undertake a transformation, it's worth it to adequately prepare for the change. The best place to begin is with the reason for undertaking a transformation.

Why Business Transformations Are Necessary

If business transformations are so challenging, why do we do them? In short, because the business environment is constantly changing, and your business must adjust accordingly. In the past decade, the environment has changed at an accelerated pace, due to advances in technology and ever-increasing customer expectations. In many instances, the business model on which the company operates no longer reflects reality.

A business transformation is your response to the changes affecting your business—it allows you to regain some control over the changing environment. A company can either be proactive or reactive in undertaking a corresponding business transformation. Proactive is preferable, but it is not always possible.

Since business transformations result in considerable change to your company, it is critical to clearly understand and express the reason(s) for undergoing the disruption (Kotter, 1995). Seventeen reasons, or motivators, will be considered here. They are arranged into three categories based on where in the business environment the change occurs: competitive environment, external environment, or internal environment. The seventeen motivators are shown in figure 2 (below)[1] and discussed in the next three sections.

Competitive Environment Motivators

The competitive environment motivators originate with respect to your competitors and their objectives to win business within your segment. The five most significant competitive environment motivators for a business transformation include underserved customer expectations, losing customers or market share, arrival of better positioned competitors, emergence of substitute products, and changes in industry structure.

Figure 2: Business Transformation Motivators

Underserved Customer Expectations

An underserved customer expectation is a product, service, or experience the customer desires but has not received. This can happen to a single company that has not kept up with the pace of customer

[1] This list of motivators is compiled from various studies on business transformations. It does not exist elsewhere in one place or organized in this manner.

demand, or it can happen to all companies serving the entire customer segment when customer demand shifts.

Sometimes customers can articulate their underserved expectations, and sometimes they cannot. For example, a customer may ask for a product or service your competitors already have on the market. There are also examples of products and services (e.g., smartphones and social media) that were developed ahead of customer expectations. In either case, an underserved customer expectation is an opportunity for you to out-service your competitors—or to be out-serviced by your competitors.

Entire industries have been created and have disappeared due to underserved customer expectations. For example, the DVD movie rental industry was disrupted when Netflix transformed itself into a streaming movie rental service.

Losing Customers or Market Share

Companies can lose customers or market share for several reasons—price, quality, product or service mix, and availability. Customer and competitor analytics can be used to determine the reasons this occurs, but then they must be addressed quickly. The nature of a transformation to address lost customers or market share is determined by the scope/speed of customer and market share loss.

Arrival of Better Positioned Competitors

Better positioned competitors are those that have created an advantage in their commercial offering or their operating cost relative to the other companies in the market segment. This occurs primarily through commercial or operational innovation from the emerging competitor. It can also occur when a company effectively lobbies regulatory agencies to provide an advantage over its competitors. Either case will result in the loss of profitability, market share, or both. Typically, the better positioned competitor has already undergone a transformation. The other competitors within the segment may respond with a transformation of their own.

Emergence of Substitute Products

Substitute products are products (or services) from another industry that offer similar form and function as those by the companies within the industry. For example, listening to live music is a substitute for going to a movie theater. The substitute product may or may not be intended to compete with the original product. Sometimes changing economic conditions can induce consumers to seek out substitutes. One example is an import tariff on foreign goods.

The substitute product generally impacts all competitors within the industry, causing a loss of sales or profitability. As in the case of the arrival of better positioned competitors, the emergence of the substitute product could have been the result of a transformation. The impacted companies in the industry may then respond with a similar transformation.

Changes in Industry Structure

Changes in industry structure include mergers, acquisitions, divestitures, and in extreme cases, breakups of an entire industry segment. Mergers and acquisitions generally provide a competitive advantage to the merging or acquiring company, including access to new products, services, and markets. Divestitures improve the divesting company's profitability or focus its strategic scope. Industry breakups are taken to mean the separation of a company into two or more pieces as is the case when mandated by a government regulatory agency.

The impact to the industry depends on the nature and magnitude of the structural change. For example, when a product distributor acquires a professional services company, that distributor can then become a better positioned competitor within that industry. Another company may divest an unprofitable business unit, thereby improving its own competitive position. However, it may also result in an opportunity for the divested business unit to be acquired by a company with a better strategic fit. In all cases, the competitive landscape within the industry is changed. The transformation may either be the change in industry structure or the response by the companies competing within that industry structure.

External Environment Motivators

The external environment motivators originate with respect to factors occurring outside of your and your competitor's organizations—and often outside of the industry segment in which you compete. There are seven significant external environment motivators for a business transformation: supply-side innovation, unreliable supply chain, shareholder pressure, government regulatory pressure, environmental pressure, geopolitical instability, and economic instability.

Supply-Side Innovation

Supply-side innovations consist of new products, services, technologies, and other supplier developments that have the potential to change a company's or an entire industry's business model. Supply-side innovation occurs (thankfully) because companies are continually developing new products and services.