Business Transformation: Driving the Optimum Value
A methodology for sustainable success
The right approach for a transformation starts with a clear understanding of how the transformation is supporting the strategic vision and business outcomes.

– Stephen G. Hasty, Jr., Global Transformation Leader, KPMG LLP
The right approach for a transformation starts with a clear understanding of how the transformation is supporting the strategic vision and business outcomes,” says Stephen G. Hasty, Jr., Global Transformation Leader at KPMG LLP. However, KPMG’s research reveals that many companies embark on business transformation only to be disappointed with the actual business results and value that the effort and investment achieves.

In fact, a third (34%) of CEOs at U.S.-based multinationals state that past transformation programs have failed to achieve the business benefits targeted at the onset. While there are many reasons why programs can fail to attain their business objectives, KPMG’s research points to three prerequisites for achieving truly successful transformation.

First, the transformation objectives must be aligned with the strategic objectives and goals of the business. KPMG’s research reveals that for a majority of companies, the approach to transformation is strategic in scope, rather than driven by a specific business function or technology implementation. Such an ambitious approach can either pay off with higher value or fail bigger. That is why the aspirational strategy guiding transformation needs to be well-conceived from the start.

Second, programs must execute effectively. Effective execution is the means by which outcomes are achieved by implementing business capabilities. However, just a third of companies consider themselves highly capable at executing complex transformations. Failure to adequately address required operating model changes is one of the chief obstacles to effective execution.

Value management is the third prerequisite for successful transformation. Metrics are indispensable guideposts for reaching the goal, yet only 14% of businesses currently define metrics and align them with the strategic vision and desired business outcomes before getting the effort underway.

These three factors are mutually reinforcing. Missing even one of them can cause a transformation effort to under-perform and under-deliver. This paper explores how businesses can increase their chances of success through attention to these three transformation factors.
To arrive at the optimum value from transformation, start in the future.

Transformative value is derived by looking ahead and setting the right strategic aspirations for the business before bringing the specifics of the transformation to life. “As a CEO, you’re always trying to look around the corner,” says Frontier Communications Executive Chairman (formerly Chairman and CEO) Maggie Wilderotter. “What’s next? Where are the choice points? Where do we have a right to win?”

Frontier, which offers broadband, voice, video and other communications solutions to homes and businesses in 28 states, will become one of the country’s largest communications providers upon completion of a transaction to acquire Verizon wireline and FiOS® assets in California, Florida and Texas in the first half of 2016.

While the traditional saying is that “execution eats strategy for breakfast,” a perfect execution means nothing if the course is wrong. KPMG’s research reveals that a majority of executives take a strategic approach to transformation (Fig. 1). Such an approach is defined as beginning transformation with a strategic plan to address a defined set of high-impact issues that require an interrelated set of projects across the business to realize the plan.

The stakes are high when it comes to getting the strategic plan right. The most ambitious transformations, those that start with a strategic plan to address a set of high-impact issues, have the highest incidence (27%) of yielding less value than expected, compared to transformations that begin with a certain function (22%) or technology (19%). Narrowly-focused transformations seem to be the safer bet.

The answer, however, is not to shy away from ambitious plans and focus narrowly out of fear of failure. Designing transformation with a competitive advantage in mind pays off. The results of regulatory-based transformation undertaken with three different approaches—ranging from a strategic approach aimed at competitive advantage to a narrow approach aimed at straightforward
compliance—reveals that the most ambitious approach yields the most value.

The most ambitious approach to regulatory-based transformation resulted in just 14% of companies reporting value less than anticipated and 28% reporting more value than expected. These results were almost reversed in the case of the least ambitious regulatory-based transformation approach, with 35% getting less value and only 13% getting more than they expected.

Scenario planning is a critical practice in setting the future strategy. All CEOs need to ask themselves: “What are the disruptors that could occur, and what do we do as a result of those disruptors?” says Robert T. Vanderwerf, Global Transformation Strategy Leader at KPMG LLP.

The next step is to identify the cross-over competitive advantage present in multiple scenarios. And to set their strategic aspirations, smart companies keenly observe not just peers within their own industries, but companies across all sectors, including new industry entrants and smaller companies. The latter is crucial, considering that scale itself is no longer a competitive advantage.

Today, smaller companies can leverage technology and analytics to achieve scale similar to their much bigger competitors, notes Vanderwerf.

KPMG’s research has shown that to stay relevant, smart companies compete with entrenched rivals as well as with newly-emerging competitors, whether within their industries or across industries. Joseph R. Swedish, CEO of WellPoint, a health insurance company, believes that companies such as Amazon and Uber have changed the way customers think about services and product delivery for all companies.

Competing with a newly-emerging competitor—which is presumably leveraging disruptive technologies or new business models—yields better results in business transformation as well. The new entrants have generally identified an area of competitive advantage over existing market participants, and they are able to successfully compete in all or some portion of the market.

Transformations triggered by new or emerging competitors lead to significantly more value than transformations triggered by existing competitors. In fact, 90% of transformations triggered by new or emerging competitors have resulted in achieving the anticipated value or more, as compared with 70% for transformations triggered by existing competitors.

“A successful transformation approach requires strategy development based on iterative scenario planning, looking at the disruptors inside and outside your industry, and developing an execution plan unique to your firm’s competitive position, capabilities and cultural environment,” says Vanderwerf. continued on next page
It’s only when you set the course—clearly answering the “why transform?” question and identifying your business outcomes and execution path—that you can realize the value from your vision. Following that, “the right value methodology starts with a clear understanding of how the transformation is supporting the vision and contributing to business outcomes. Future-state scenarios are changing rapidly. Your business and operating model designs must allow for agility during execution, to make sure you adapt to the changing environment,” says Vanderwerf.

“Our starting point [of any transformation] is to define what is our why. Then we transition into defining high-impact issues,” agrees Tupperware CEO Rick Goings.

KPMG’s research found customer demand to be the top trigger for transformation over the next three years. “Why transform?” will most often be answered with: “to meet customer demand” (Fig. 2). In this type of transformation, the ultimate value lies in delivering on your value proposition to your customers.

National Instruments helps scientists and engineers automate the world around them and develop smarter products and technologies: “the convergence of technology among networking, processing and software that enable people to do things in their domains that they weren’t able to do before,” says Eric Starkloff, NI’s Executive Vice President of Global Sales and Marketing. “We are trying to teach our customers a new way of solving an old problem.”

Mapping a customer-driven transformation starts at the end result—the delighted customer. “You need to look at the journey—the value chain that leads to that ultimate customer value—and how it’s achieved through the organization,” says Vanderwerf. “A lot of this comes down to connecting the dots from the strategic aspiration—the delighted customer—and the execution of that aspiration through the business and operating models.”

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How capable are organizations at executing transformation? While about two-thirds of companies believe that their capabilities in these areas are above average, just a third consider themselves highly capable (Fig. 3).

Capabilities correlate sharply with value realized from transformation initiatives. In fact, low-performers’ transformations fail—or realize less value than anticipated—twice as often as those of highly capable organizations (40% versus 20%).

What stands out is that executives believe their organizations’ capabilities are higher in terms of strategy, and lower when it comes to developing business and operating models or extracting value from transformation. These findings correlate with KPMG’s observations that execution is the hardest part of transformation.

Translating strategy into action is a tall task. It demands a strong interconnectivity between developing strategy and developing the approach for its execution. “All organizational capabilities, from the customer through the value chain, must move in sync and be driven by the same ultimate strategic goals to achieve success,” says Vanderwerf.

This interconnected design of the transformation must be clearly understood and communicated. “What is challenging about the vision is finding a way to communicate it at an appropriate level so that the entire organization can get a feel for what it is and what it means,” says Greyhound CEO David Leach.

“The execution can definitely be harder. We are a strong, vision-driven company. The challenge is that different groups can interpret that [the strategic vision] in different ways. They believe they are executing the strategy, but in fact it can be that they are slightly off because they have a different interpretation of it,” agrees NI’s Starkloff.

Vanderwerf notes that the growing disconnect between strategic vision and execution outcomes is leading some CEOs to get closer to the execution of the business. Far from lacking trust in their management team, these leaders understand that to realize their strategic vision, they must quickly achieve cultural acceptance, integrate their organizational capabilities, and be flexible in adapting to the current competitive environment. To this end, leaders need to make sure that all aspects of a transformation remain aligned and in support of the strategy. “This ensures that there is one voice, one strategy, and everybody is pulling in the same direction to achieve the ultimate value outcome, and that they understand how everything fits together,” he says. “In this highly competitive, fast-moving environment, there is no room for wasted effort, dead-ends or delays.”

At NI, aligning everybody around the vision and making sure that it is being executed on the ground is at the forefront. “We have been in a process of communicating the strategic vision and making sure that the top-level strategic principles are understood. We have to get into the meat of what it means for each group and department,” says Starkloff.

Figure 3: Transformation capability
In regards to business transformation, my organization is highly capable at:
What is the goal of your transformation? What is your approach?
We are repositioning the business into the unconventionals (tight/shale oil and gas onshore exploration opportunities). We are working on three elements of the transformation: repositioning the portfolio, enhancing our capabilities and enhancing the culture. Other integrated oil and gas companies choose to keep the unconventionals business separate, spin it off or run it as a regular piece of their whole organization.

We made a conscious decision against the spinoff. Part of the motivation behind this decision is to create an opportunity for the whole organization to learn about becoming nimble from the unconventionals experience that we are working on. At the same time, this will allow the unconventionals business to leverage some of the strengths that the mothership brings, such as value chain integration, the global scale and the ability to bring technology to the table.

What are the challenges and benefits of this ambitious approach?
The biggest challenge is that the control framework that works for the totality of Royal Dutch Shell does not necessarily fit a nimble unconventionals business. The quicker alternative would be to spin off and create our independent control framework. But it’s proving to be worth it. We’re already seeing some of the applications we developed being adopted in other parts of global Shell. That’s the kind of synergy that we hope to gain.

Where are you on the transformation journey?
The first stage was getting the portfolio where it needed to be. We completed it in less than a year. We reduced the number of active exploration plays in half. We exceeded the value we expected to get for those assets. The other element, happening in parallel, was creating a more cost-competitive, but more capable, organization. Cost leadership was a big piece of that. The last element, which we are starting to work on now, is culture.

How are you measuring progress?
We are measuring outcomes and progress-related metrics, roughly half and half. We are measuring progress on milestones and implementations. Over time, my expectation is that we will have fewer progress-related measures and much more outcome-based measures. We probably measure a bit too much. I’ve got a philosophy that if you can’t measure it, you’re not going to get it.
The top barrier to a successful transformation initiative is underestimating the significance of the operating model changes necessary to effect transformation (Fig. 4). And interestingly, other top barriers are all components of an effective operating model.

“Companies are not doing as good a job as they could on connecting their strategic vision with their business and operating models,” says Todd Lohr, Global Transformation Enablement Leader, KPMG LLP. “Often organizations look at their operating model as a cost to reduce versus an asset to create value. Organizations should make a direct connection between their strategic and financial aspirations and the set of integrated, aligned and motivated capabilities that will achieve it.”

At Royal Dutch Shell, the strategic outcome of entering the unconventionals business was the addition of a substantial new supply source to Shell’s portfolio. Although the market and business model were the same, making this supply source work required a significantly different operating model and set of capabilities to achieve the value. (See sidebar on page 6)

That is the case at Greyhound, where the strategy of becoming a technology-savvy, customer-demand-driven operator has led to new business and operating models. Analytics-based management of seat inventory resulted in prices that reflect the changing demand by day-of-week and time-of-day. This in turn enabled the company to offer less expensive tickets while improving profitability. “Modern technology has enabled us to change our business model from an on-demand, walk-up business to one more similar to airlines,” says Leach. “Furthermore we are embracing new web and mobile technologies to better serve our customers while they shop, and before, during and after they travel.”

Frontier Communications follows through on its vision of being a leader in communications by employing an operating model tailored to the task at hand. Frontier recently acquired AT&T’s wireline, U-verse® and broadband operations in Connecticut. The acquisition strategy was in line with leadership’s philosophy of focusing on where the company can win.

But Frontier does not take winning for granted. To succeed at execution, Frontier employed a hands-on approach by dividing the state into five “area markets,” each with a general manager with full P&L responsibility and dedicated staff. The transformation required converting all AT&T systems, including more than 700 different platforms, and serving 1.4 million new customers. “We come from the perspective that some things are going to go wrong,” says Wilderotter. Frontier’s proactive solution: “bubble workforce,” or doubling or tripling, as needed, the number of employees to serve customers going through conversions.

“Frontier is an example of a business looking at all components of its operating model, and aligning each with the strategic vision of the organization,” says KPMG’s Lohr. “Without that alignment, we’ve found that even the best implementations can sometimes fail to extract as much value as possible from the transformation initiative.”

Indeed, many companies still need to improve their expertise at creating the right operating model. Transformations triggered by the need to simplify an operating model have a high potential for failure: 31% end up realizing less value than anticipated. When designing an operating model—and deciding whether to focus on efficiency or quality—it’s worth remembering that orientation toward efficiency more often disappoints in terms of value realization than quality-based orientation (34% versus 12%).

Figure 4: Top five barriers to a successful business transformation

- 38% Underestimating significance of operating model changes
- 38% Existing corporate culture
- 32% Inadequate or legacy technology
- 32% Resource constraints
- 28% Applying appropriate metrics

Percentage of respondents who answered yes.
The goal of transformation is to achieve the ultimate value—reaching the strategic vision—not simply delivering on metrics. That is not to say that metrics are unimportant. They are critical guideposts to achieving the value of a transformation, yet only 14% of businesses currently define metrics and connect them with the strategic vision and desired business outcomes before getting the effort underway.

At the same time, metrics cannot be the sole driver of transformation or be perceived as such by the organization. People are moved to action by the strategic vision, not tactical guideposts, and leaders are responsible for clarifying and connecting the vision behind the transformation to each aspect and person within their organization. The proof is in the results: metrics-driven efforts are more likely to fail—or achieve less value than anticipated—than leadership-driven transformation initiatives (31% versus 20%).

Thus, the role of metrics is to serve as a set of execution guideposts. Taken together, metrics need to form a map within the operating model, aligned to desired business outcomes and the organization’s ultimate strategic vision, even as the business environment and organization evolve.

Intermediate metrics, such as process efficiency and cost reduction are important. However, organizations focused solely on efficiency and cost are missing essential parts of the value chain. “The right approach should be about business value, not simply cost,” says Hasty. “It is critical to keep transformation metrics directly connected with desired business outcomes and the ultimate strategic vision to deliver maximum sustainable value.”

Manage for Value

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Conclusion

Value is the final prize of a business transformation. KPMG’s research, analysis and experience points to the following conclusions about how to best drive value:

Look to the future when defining the strategy and business outcomes of your transformation. Consider the competitive advantage that it will afford you. Observe companies from all industries and all sizes. Customer demand will be the number one transformation trigger over the next three years, and there is just one customer—a customer shaped by the whole universe of businesses, not just those in your sector.

Align, integrate and communicate the strategy. Making sure that everybody is exactly on the same page is the first step to a successful execution. Some of your employees may only think they are implementing the desired strategy.

Translate strategy into action. If the dots are not connected on the ground, transformation won’t happen, even if everybody is clear about the value being sought. Once set in motion, if designed properly, the interlocked elements of the operating model should lead to sustainable value.

Directly link metrics to your strategic vision and desired business outcomes. Think of them as guideposts, designed to keep you on track and take the measure of your progress. Remember that people are not inspired merely by following metrics. They need a clearly-defined strategy and strong leadership.

Methodology

This report is based on a survey of 963 executives from U.S.-based multinationals in all major industries. Sixty-seven percent of survey respondents were C-level executives, including 28% who were CEOs. Company revenues ranged from $1 billion to more than $100 billion. The biggest single group of executives, 30%, represented executive management; the next two largest groups came from technology (19%) and finance (17%).

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How KPMG can help your business transform with focus and agility

Helping clients arrive at the optimum value from their business transformation journey begins with an in-depth understanding of the industry in which they work. With our breadth of industry experience, KPMG helps clients discover actionable insights across sectors and businesses of all sizes.

Strategy is the foundation of business transformation. Too often, the value from transformation goes unrealized due to disconnects between business model strategy, operating model execution, and the complex issues that companies face when implementing change. The accelerated pace of change means businesses need a focused and agile strategy to drive their transformational agenda.

Our value-based and metric-driven business transformation approach allows clients to develop and align their strategic and financial objectives to required business and operating models, organizational culture, measures and incentives, and the capability to change to connect vision to value.

KPMG understands the complexity and the significance of continual model refinements necessary to effect transformation across people, process, technology, data, and risk management. Our Value Delivery Framework guides transformation delivery, and it is supported by a tightly-integrated, global, and unified approach to connect strategy with execution and achieve the optimal value from transformation.
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