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Lessons from digital telcos:
Five initiatives to improve business performance

McKinsey research reveals the importance of placing digital bets in several core areas that can help companies streamline IT operations and enhance the customer experience.

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Many companies are learning that where they place their digital bets can have a profound impact on their overall business performance. A recent McKinsey IT benchmarking study of 80 telecommunications companies worldwide found a strong correlation between profit margin and five select areas of IT: robust customer analytics, digitization of order management, self-service customer relationship management, a simplified IT-application landscape, and automation of IT-infrastructure management. While correlation does not necessarily imply causation, we've observed that the telecom companies with digital capabilities in these five areas boast a profit margin of 43 percent, while those with less digitization have a profit margin of 21 percent, on average.[1]

Many telecom companies have benefited from investments in digital. One in Asia, for example, was able to reduce the number of customer calls by a million a month by providing online "self-care" through services such as Twitter and Facebook. Companies in other industries also have improved their business performance by focusing on one or more of the five areas flagged by our benchmark analysis. Since 2004, the US retailer Nordstrom has been rolling out digital programs—for instance, introducing mobile point-of-sale technologies so customers don't need to stand in line at cash registers, establishing a personalized customer-loyalty program, and launching constant improvements to its online

Takeaways

Research with telecom companies suggests that choosing the most promising areas for IT investment may help companies realize improvements in revenue, cost performance, customer satisfaction, and business agility.

The strongest correlation between profitability and IT investment occurred in five areas: robust customer analytics, digitization of order management, self-service customer relationship management, a simplified IT-application landscape, and automation of IT-infrastructure management.

Success is likelier when companies forgo an all-inclusive transformation in favor of rolling out digital changes in separate projects selected to suit the company's current capabilities, technologies, skill sets, and functionalities.

sales channels. In part because of these efforts, the retailer has almost doubled its revenues and its market cap over the past ten years.

Why are these five digital capabilities proving to be particularly effective? In this article, we consider each of these elements in a company's digital-transformation program, as well as their critical role in revving up business performance. The framework may prove useful for companies seeking to gain the same kind of advantages Internet giants now enjoy because of their digital architectures and operations—that is, more efficient processes and workflows, greater innovation opportunities, higher revenues, and greater profitability.

Five digital capabilities of highly profitable companies

Companies in all industries are struggling to implement digitization across functions. Obstacles include rigid legacy systems, overly complex IT architectures, and data sources that are not integrated in any way. Given all the variables to contend with, executives typically aren't sure where to start with their digitization programs. Our benchmarking research with telecom companies suggests that moving the needle in the five core areas above is a good start. The findings reflect current realities in the telecommunications industry, but our experience suggests that the implementation of these digital practices can have similar effects in other consumer-facing industries, where reliability of services and

quality of the purchasing experience can be core differentiating factors.

1. Establish robust customer-analytics capabilities

As most companies are quickly learning, the ability to gain a 360-degree view of the customer (within the bounds of consumer privacy laws and regulations) allows marketing, sales, and other customer-facing functions to make more precise, data-driven decisions that cut down on guesswork and wasted resources. Our benchmarking study found that high-margin telecommunications companies tend to outperform peers when it comes to data mining and otherwise gaining insights from collected customer information. One Asian telecom company, for instance, is using cloud-based analytics to help customers gain insights from the point-of-sale data they collect. Customers can use this information to improve shop-floor layouts and schedule staff more effectively. By offering this capability, the telecom company has been able to attract more customers, thereby significantly increasing its market share.

Companies in other industries also have seen improved business performance from advanced data analytics. One retail bank, for instance, found through data analysis that first-time homebuyers were more likely than other homebuyers to abandon an online mortgage-application process midstream. Therefore, the bank's marketing department has partnered with the call center and IT department to

connect applicants with customer-service representatives via live mobile or web chat. Customer-service representatives can initiate a chat with a customer after a certain period of inactivity, and thus can help reduce the rate of abandoned applications.

Meanwhile, a US hospitality company uses real-time customer data to determine which hotel bookings are up or down over a given weekend, as well as the behaviors of critical customer segments. If analytics reveal a decline in average stays or in the number of visitors traveling from a typically high-volume feeder location, marketers can respond with tailored offers, discounted room rates, or other benefits. At the same time, the company has been able to protect revenue by using targeted, rather than mass, discounts.

2. Digitize the order-management process

Because of their interactions with born-digital online companies such as Amazon and Alibaba, customers have come to expect speed, convenience, and accessibility in the purchasing process. Companies in all industries are therefore seeking to replicate the Internet companies' order-management experience, which involves centralization of data and automation capabilities.

The top-performing telecom companies in our benchmark, for instance, are using automated order-management systems to link everything from the initial capture and validation of service requests to fraud checks, payment authorizations, billing, and customer communications quickly and cost-effectively. Many telecom companies, for example, have introduced full-service smartphone apps that can guide customers to the choice of the best tariff, given their needs and behaviors, and can automatically order and activate the new tariff. Adoption of these apps has led to a significant decrease in customer churn and in the cost of serving customers through call centers.

Companies outside of telecommunications also have seen improved business performance after incorporating automated order management into their operations. Several retail banks, for example, have introduced one-touch order buttons in their online-banking applications. One Italian bank has launched a "pay in installments" option next to payments above a given threshold; this allows the customer to turn a given payment into a short-term loan with fixed monthly payments and higher interest than most loans. The loan order is initiated by the customer and processed automatically, without the need for manual approval.

3. Digitize the customer-relationship-management process

Digital technologies have made it easier than ever for customers to engage with companies, yet harder for companies to track, manage, and inform those interactions. Consider that in 2003, less than a quarter of all shoppers buying auto insurance used the Internet to gather information; today that figure exceeds 80 percent, with two-thirds of all insurance quotes now delivered online.[2] Where banking customers once engaged almost exclusively with their local branch, today 65 percent of them interact with their banks online, via their mobile devices and other channels.[3]

The growth in multichannel access puts a premium on effective customer-relationship-management (CRM) systems—not just to track customers' digital footprints but also to reduce costs, enhance customer satisfaction, and improve brand advocacy and differentiation. Digital CRM is helping the top-performing telecom operators in our survey achieve greater cost efficiency and customer satisfaction.

The use of online forums and lists of frequently asked questions, for instance, costs the average telecom company just 12 percent of its typical call-center baseline,[4] while providing customers with a convenient, accessible source for answers and advice. In the case of one company, community forums and sophisticated search capabilities have made it possible to address 99.5 percent of all customer questions, with an average response time of 1.5 minutes.

Meanwhile, the US jewelry retailer Alex and Ani uses a digital CRM platform to track customers' activities across the online sales channel and stores. Marketers can analyze shopping baskets to determine what item a shopper bought first and which channel led the shopper to discover the brand. Marketers can then use that information to anticipate the sort of products and outreach that might appeal to microsegments of customers. In part because of this innovative digital CRM approach, the retailer's revenue grew by more than 5,000 percent between 2011 and 2014.[5]

4. Streamline the company's application landscape

Aging and complex legacy IT applications are among the biggest obstacles for companies seeking to compete against nimbler digital players. Such systems are typically built up over many years (and leadership changes) and comprise a landscape of sometimes incompatible stacks of technologies. Decisions about what to retain and what to upgrade are complicated when IT organizations begin to map all the interdependencies among functions and systems. The top-performing telecom companies in our survey have streamlined their IT landscapes— removing redundant platforms, automating core processes, and consolidating overlapping capabilities. It wasn't an easy undertaking, but such improvements allowed a South American telecom company to free up the equivalent of 31 percent of its full-time employees. In addition, the company was able to gain a unified view of

customer billing, resolve customer issues faster, and reduce the rate of service errors.

5. Standardize and automate the company's IT infrastructure

Inefficient IT processes are another impediment for companies seeking to compete successfully against digital companies and improve business performance. As companies collect more customer information and need to transmit it in real time across applications, they require more storage and computational power. But rather than add more components to an already-complex system, companies would do well to pursue automation of what they already have. Indeed, the top-performing companies in our benchmark have pursued simplification and automation of various backbone IT processes and systems—for instance, automating server deployments, load balancing, and service-ticket management. These changes not only have generated significant cost efficiencies for those companies but also have given the operators much greater flexibility in terms of service capacity and load volumes. In emerging markets where some fast-growing telecom operators are adding as many as one million to two million subscribers per month, the ability to automate capacity, server throughput, and storage has allowed senior managers to focus on business growth rather than scramble to augment their IT infrastructure.

Standardization and automation efforts are also paying off in the banking industry. A recent McKinsey study found that IT standardization (in applications and infrastructure) and improved IT-architecture governance were correlated with a 4.7 percent reduction in expenses for a sample of European banks.[6]

Implementing the five digital practices

To implement these five digital practices, senior technology and business managers will need to take stock of their current capabilities,

technologies, skill sets, and functionalities. Every company will be coming at the digital transformation from a different starting point, depending on company maturity, strategic positioning, and corporate aspirations. It is therefore important to establish a baseline: What is the current level of digitization in the company? Compared with competitors, where are the digital pockets of excellence, and where are the shortcomings? Various diagnostic tools and 360-degree assessment approaches are available for companies to use in assessing their digital quotient and creating a baseline.[7] But perhaps the most important task will be getting IT and business leaders to meet and address questions related to opportunities, resources available, and potential risks. Based on those conversations, the company can plot a transformation path, prioritizing the areas that stand to deliver the greatest impact most immediately.

We've seen companies attempt to address all five digital practices in a single megaproject, but experience suggests that success is likelier when companies roll out digital changes in smaller, separate projects. A European telecommunications company, for example, is carrying out a transformation program over the course of seven years. It is rolling out 20 discrete application projects, each with a detailed business case, and all within a common, clear architectural framework to reduce complexity. In just the first four years of this transformation program, the company has been able to realize an 18 percent reduction in total application spending and a 50 percent reduction in number of applications—all of which happened while the company was implementing a steady flow of new digital products and services.

The potential benefits from digitization are by now well known, but the implementation of digital programs remains a vexing problem for most IT executives. By focusing on a narrow set of high-impact digital practices, companies can speed their transformation where it will contribute most to customer satisfaction and business performance. ◼

[1] The findings are from the 2015 Telecom IT Diagnostic by Horizon360, a McKinsey Solution. The research was conducted through an Excel-based survey and in-person interviews. Participants included telecommunications operators from Africa, Asia–Pacific, Europe, Latin America, the Middle East, and the United States.

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[3] Albert Bollard, Neel Doshi, and Marukel Nunez Maxwell, "The future of US retail-banking distribution," August 2014, mckinsey.com.

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[7] Tanguy Catlin, Jay Scanlan, and Paul Willmott, "Raising your Digital Quotient," *McKinsey Quarterly*, June 2015, mckinsey.com.

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