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Scaling Digital Business Requires an Enterprise Operating Model Perspective

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Published 7 May 2019 - ID G00383040 - 19 min read

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All digital transformation strategies require significant changes to business operations. CIOs, with their business architects, can use our enterprise operating model framework to help C-suite and functional leaders understand the extent of change necessary to deliver digital strategy at scale.

Analysis

In most traditional (not-born-digital) organizations, the gap between digital ambition and reality is large. [1] CIOs should close the gap by engaging the C-suite in conversation to clarify the digital ambition and strategy, and assess the impacts to the business and operating models. Is the goal to transform the business model or to optimize the existing one? That answer has huge implications, particularly for enterprisewide business operations.

In 2018, Gartner introduced its business model framework. [2] Business models support the strategy by providing a blueprint for *what* value the entity creates and delivers to customers while retaining some value for itself. However, strategy and new business models almost invariably fail in execution due to poor understanding of their ramifications on business operations. In this note, we introduce our conceptual framework for an enterprise operating model.

Operating Models and Business Models

An operating model is the complementary blueprint for *how* value will be created and delivered to target customers. An operating model brings the business model to life; it executes the business model. A future-state operating model underpins the execution of the business model and the strategy. Both business and operating models are critically important and must be redesigned in a complementary fashion, reflecting the digital strategy and goals of the entity.

Business capabilities are the linchpin that links a business model to an operating model. Changes in business capabilities *always* trigger changes in the other components of the operating model (see Figure 1).

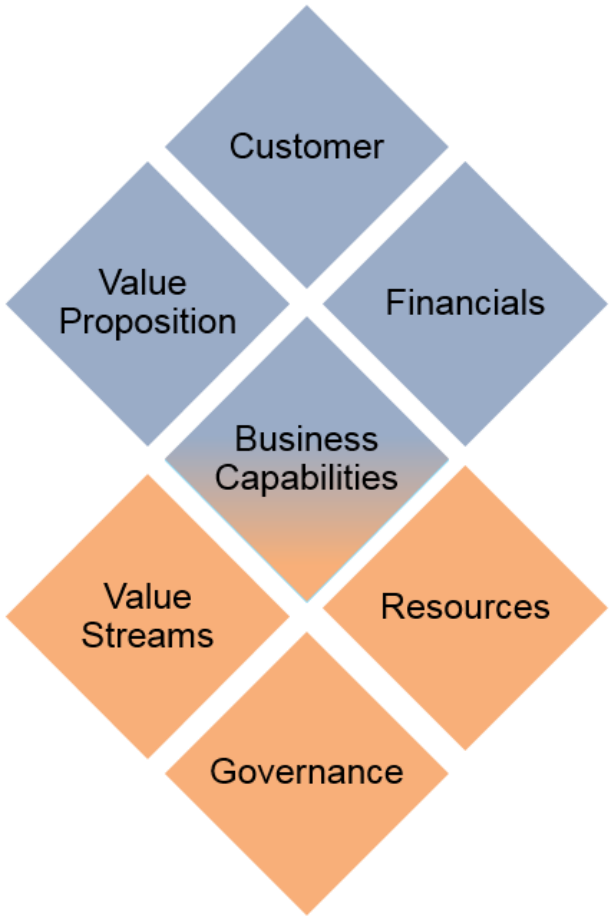
Figure 1. Business Capabilities Link Business Models to Operating Models

Two Key Frameworks Defined

A **Business Model** reflects ***what*** value the entity will create and deliver to customers or constituents.

An **Operating Model** reflects ***how*** the entity creates and delivers that value.

Business capabilities are the linchpin that links these together.



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Source: Gartner (May 2019)

An operating model provides a disciplined way to:

- Design, acquire and operate a set of business capabilities that enable the entity to deliver its value proposition or mission to its target customers or constituents.
- Define value streams, processes and metrics to ensure that customers and constituents experience the value of the entity's products and services.
- Develop and acquire the assets, tools, technologies, skills, funding and other resources needed to support the entity's business capabilities and value streams.
- Create a governance framework that defines decision rights related to both corporate conformance and enterprise performance, as well as investment and risk criteria. This framework guides the way the entity fulfills its mission and value proposition for customers or constituents.

In most entities, enterprise business operations reflect an historical patchwork of changes in leadership, strategy and ownership; and investments in physical facilities, machines, equipment and technologies. These historical investment layers and changes mean that business operations no longer reflect a cohesive design across the enterprise. Consequently, business operations from an enterprise perspective are ill-prepared to handle the higher pace of change, adaptability, interdependencies triggered by digital innovation and scale required of a digital business. An extensive, coherent and integrated set of changes to the enterprise operating model is necessary to realize the entity's digital ambition.

Before such changes can be made, a shared understanding of the current state of enterprisewide business operations is needed. All entities have an enterprise operating model, (though few call it out explicitly). When transforming to digital business, someone should thoughtfully redesign the *enterprise* operating model, not just let each business function run their own operations by chance and poor design (see Note 1). Without a model of enterprise business operations, executive leaders cannot discuss potential changes, interdependencies and reach agreement about trade-offs they are or are not willing to make to close the gap between their digital ambition and the status quo.

Leading CIOs or a COO (if this role exists) have a vested interest in, understand and have influence over enterprise business operations. Senior business executives tend to understand the business from their functional perspective only. For these reasons, CIOs are well-positioned to help C-suite executives and functional business leaders comprehend business operations from the enterprise perspective. Furthermore, CIOs with a strong business architecture practice are in a great position to lead the effort to redesign enterprise business operations for digital scale and orchestrate the changes needed across organizational boundaries to realize the digital ambition.

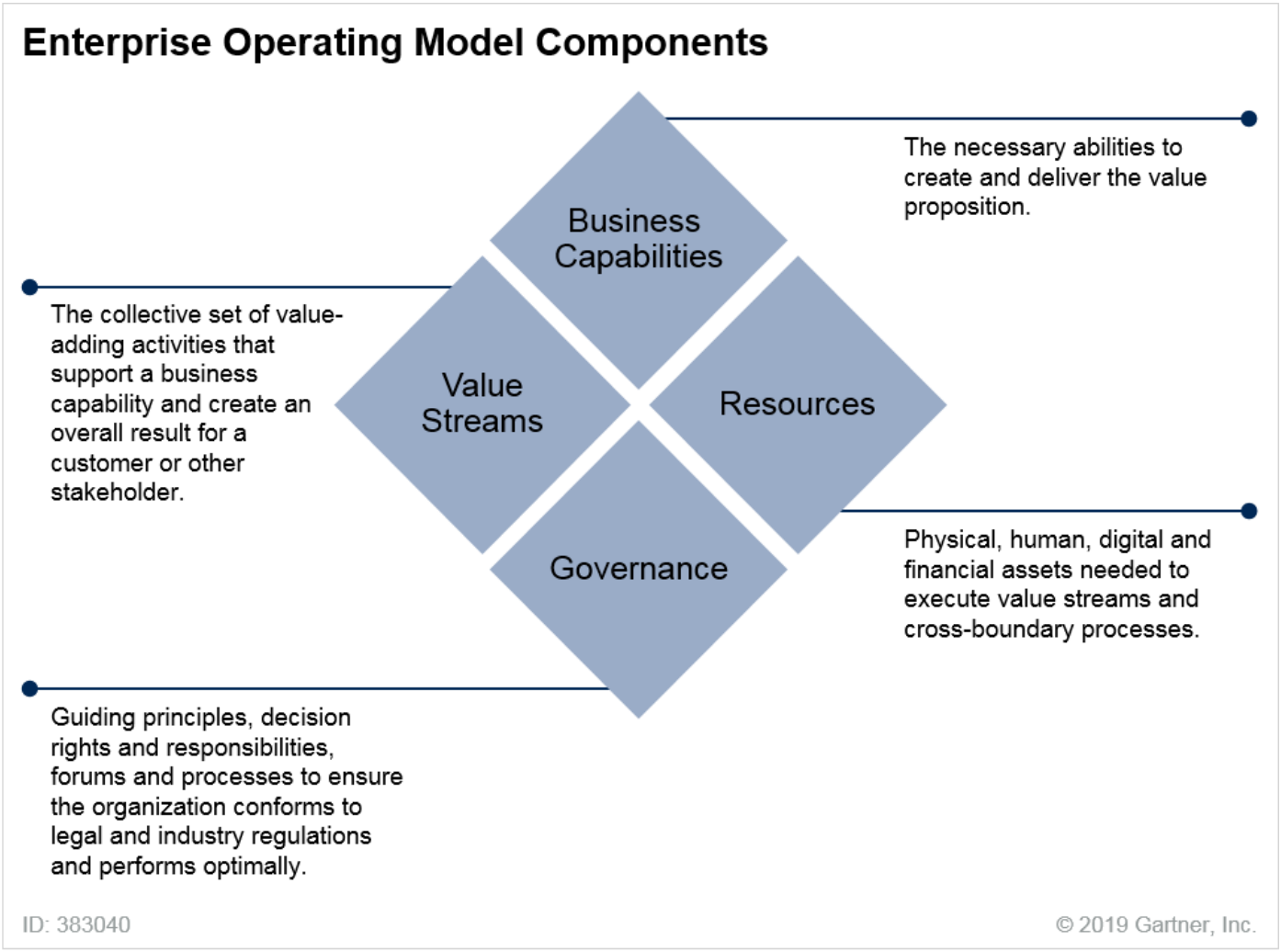
In this research, we introduce Gartner's enterprise operating model framework as a tool for CIOs to use along with their business architects to facilitate discussions around the most optimal business design to achieve digital ambition and execute digital strategy. This framework can be applied whether the entity wants to optimize its current business or establish new digital business models.

Enterprise Operating Model Components

Similar to our business model framework, the enterprise operating model can be described using four major components (see Figure 2). Although we are introducing this framework as the *enterprise* operating model, conceptually it can also be cascaded to the various business functions' domain-specific operating models. Business domain-specific operating models reflect similar interdependencies across these four components, Similarly, the enterprise operating model concept is applicable to an enterprise view of the information and technology (I&T) operating model.

Furthermore, the relationship between a business model and an operating model is rarely one-to-one. For example, in supply chain industries, a single supplier often serves multiple and different market and customer segments. This can require different operations aligned to the various segments, some of which may require shared business capabilities. Upcoming research will expand on the relationships of business models and operating models.

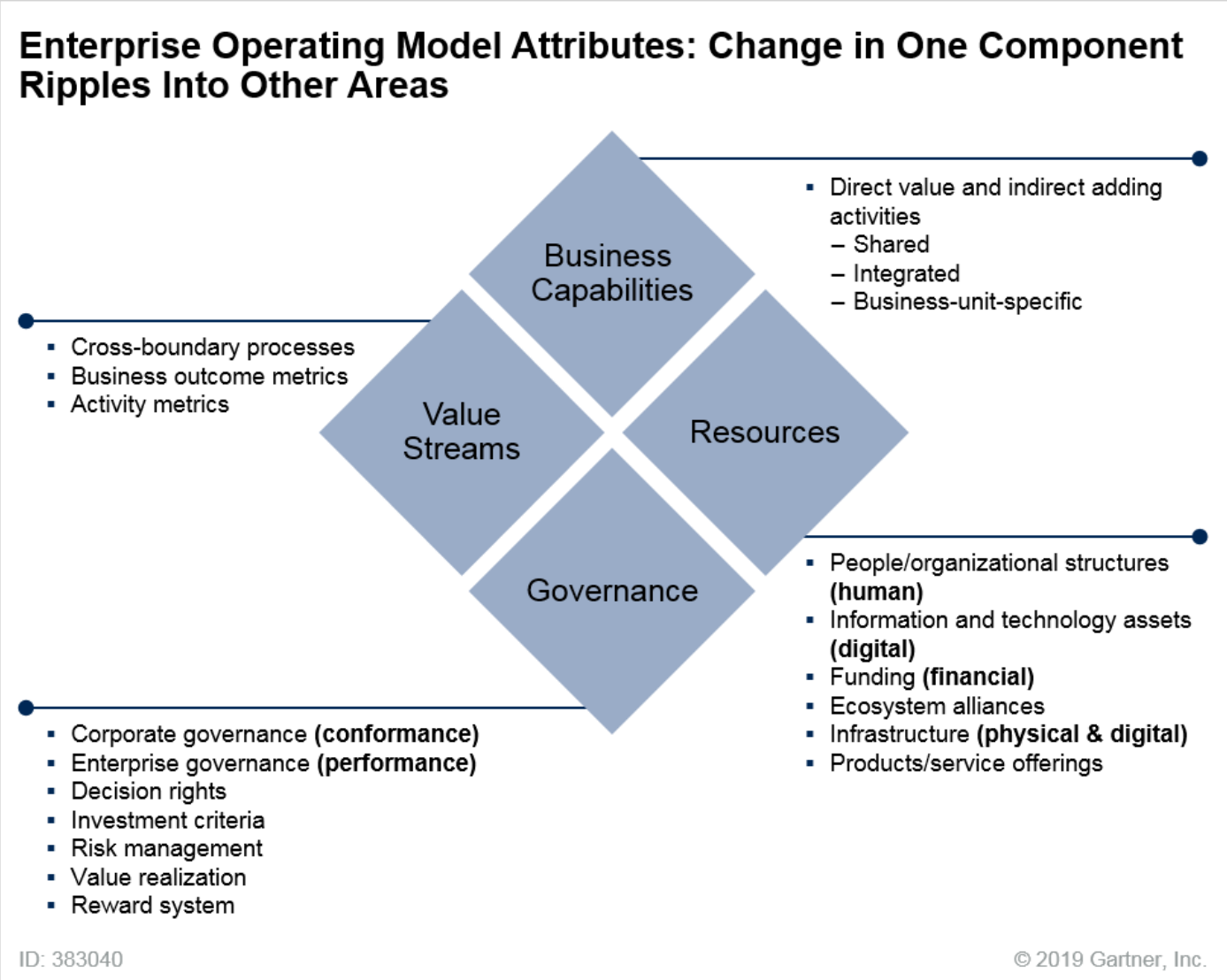
Figure 2. Enterprise Operating Model Components



Source: Gartner (May 2019)

To facilitate discussions about specific change initiatives, a deeper, attribute level of detail is required. Attributes should be used as a checklist to evaluate the ripple effects of potential changes to fulfill the digital ambition. Figure 3 reflects Gartner's recommended alignment of attributes by component. As this is a conceptual framework, clients may decide to align these attributes differently based on their entity's unique context. Regardless of alignment choice, attributes should not be dropped from consideration.

Figure 3. Enterprise Operating Model Attributes



Source: Gartner (May 2019)

Such conceptual operating models can be further decomposed into greater degrees of granularity appropriate to a purpose. For example, a business function may want to break down its domain-specific operating model even further to facilitate discussions about resource optimization or process re-engineering.

Enterprise Operating Model Components and Attributes Described

Business Capabilities

Business capabilities are organizational abilities necessary to deliver business outcomes linked to customer-perceived value. They are activities that must be done to support the value proposition. Business capabilities are also anchored to the strategy. The business capabilities defined by the business model are operationalized in the operating model; it is a shared component across both models. To create and deliver value, every enterprise must acquire and use its business capabilities effectively, since they consume resources. Business capabilities typically only change when the business strategy or business model change. Business capability modeling is a well-established technique of business architecture (see Note 2).

Digitalization provides opportunities to significantly enhance the performance of business capabilities and even enable completely new capabilities. Applying advanced digital technologies can enable the organization to create a new strategy and a new value proposition that transforms the business model. For example, implementing artificial intelligence leveraging existing data sources might support a new preventative maintenance capability. Location-based services in smartphones enabled Uber to implement a "request pickup from anywhere" capability that is the foundation of its business model.

Applying newer digital technologies to optimize or transform the business triggers the need to revisit the role of I&T assets, channels and capabilities. In either situation, CIOs should reassess the I&T operating model and plan to transition to one of two models:

- A service-optimized I&T operating model, which is appropriate for digital business optimization strategies (See "Run IT Like a Business by Applying the Service-Optimizing I&T Operating Model Pattern.")
- A value-optimized I&T operating model, which is appropriate for digital business transformation strategies (See "Monetize Your Business by Adopting the Value-Optimizing I&T Operating Model Pattern.")

Applying digital technologies also allows enterprises to participate in external ecosystems, which add value from new partners (see "The Future of Your Business Ecosystem in the Age of Digital Business: A Gartner Trend Insight Report").

These examples of technology-enabled business capabilities are increasingly offered as digital products to existing and new customers. (For more on I&T-enabled business capabilities and products, see "Predicts 2019: Product Centricity Helps Close the Strategy Execution Gap.")

To establish a shared understanding of enterprise business operations across the C-suite and executive leadership, highlight direct and indirect value-added business capabilities. (These are often labeled "Level 0" business capabilities).

- Direct value-adding activities create value for customers or stakeholders by themselves. They are typically customer- or stakeholder-facing.
- Indirect value-adding activities allow direct activities to run smoothly.

Gartner recommends the verb-noun approach to labeling business capabilities. The noun-verb approach makes it too easy to mirror the current organizational structure and can reinforce siloed thinking. In addition, the noun-verb format is passive, undermining the importance of the activities that enable the capability. So, for example, we prefer the term "service customers," to label the business capability, rather than "customer service." Business capabilities can be standardized

across the entity, integrated and shared across parts of the entity, or be completely unique to one part or line of business within the entity.

Resources

The resources component includes physical, human, financial, and digital information and technology resources necessary to enable the business capabilities. Product and service offerings listed in the business model cannot be created and delivered without adequate funding/investment, the right technologies, skilled talent, supporting organizational structures, and infrastructure. We include the product and service offering itself — aka the "finished good" — in the resources component of the operating model because any business model decisions related to the product/service have to be operationalized.

For example, a business model decision to extend the value proposition of an existing product/service with data analytics as a service requires a new delivery capability. Our earlier example of preventative maintenance analytics would typically be delivered via a digital channel such as a cloud SaaS application. The digital channel is part of the infrastructure needed, and the analytic SaaS application is the "product" in the operating model. Marshaling the right resources can also require establishing alliances and partnerships with ecosystem partners.

Digital business operations at scale are made possible by leveraging technology platforms, services and digitalized capabilities. Some digitalized capabilities will be treated as products, not projects. (For more on the implications of digital products, see "Moving From Project to Products Requires a Product Manager" and "Predicts 2019: Product Centricity Helps Close the Strategy Execution Gap.")

Value Streams

Simply defined, a value stream is a set of activities required to deliver a product or service to the customer or constituent. If the business capability is defined as "service customers," the value stream includes all the major activities that must occur to service a customer. At the highest level of abstraction, often labeled as "Level 0" models, value streams cross organizational boundaries. Multiple business capabilities might come together to create a value stream. A supply chain might be considered a value stream between suppliers and a manufacturer, and therefore would include multiple capabilities like "fill order," "pack order" and "ship order."

Value streams are further defined through processes (workflow diagrams) that specify more details for how value is generated. Process maps include the sequence of inputs, activities, decisions, outputs and resources used. Processes may be focused on physical, digital and financial assets (including data), activity flows, or a combination of these.

Since value streams should deliver desired business outcomes, we also include business outcome metrics in this component. These would be key performance indicators (KPIs) that measure progress toward strategic goals. We also include business activity metrics, which assess how efficiently and consistently the value stream helps realize those outcomes.

Governance

Governance concentrates on who makes what decisions and what they must consider when making them. If processes describe what an organization wants and expects to happen, governance establishes the accountability and oversight to ensure that occurs. Management processes, such as budgeting and planning, are often considered part of this component.

Decision making is rarely simple for any enterprise, especially when resolving conflicting enterprise priorities and competing demands. Thus, both corporate and enterprise governance are reflected in this component.

- Corporate governance is a board-level issue that focuses on conformance and fiduciary responsibility.
- Enterprise governance focuses on the performance of enterprise assets.

The key attributes of enterprise governance are establishing stakeholder decision rights, investment criteria, and risk management policies and guardrails. These are all related to strategy, investment return and value realization. (Note: I&T governance falls under enterprise governance. See "Enterprise IT Governance, Part 1 — Obtaining a Mandate and Establishing the Scope.") Good governance will drive connected and evidence-based decision making across conformance and performance aspects to advance the business's goals. The old adage, "You get what you measure," holds true. Metrics, reward incentives and audits put in place through governance provide a key mechanism to ensure that an operating model reflects what happens in practice.

Use the Enterprise Operating Model to Drive Consensus on Needed Changes From the Enterprise Perspective

CIOs have an enormous opportunity to demonstrate personal leadership by using these tools to establish a common understanding across the C-suite of operational complexities and the extent of changes necessary to close digital ambition gaps. The CIO's goal is to drive coherence into enterprise business operations. The CIO (aided by business architects) should foster a shared understanding of trade-offs and drive decisions to ensure that stakeholders' requested changes reflect the best option for all.

The recommended technique is to facilitate a meeting with the executive stakeholders and pose questions to the group to highlight interdependencies. Use the enterprise operating model framework's attributes as a checklist to support the conversation. We recommend starting with business capabilities. The interdependencies between the four components will quickly become obvious and the conversation will naturally flow across the four components.

1. Start by probing the impacts to the business capabilities component.
2. With an understanding of business capability impacts, next consider impacts to resources or to Level 0 value streams.

3. Finish with any governance impacts.

In organizations where the CIO lacks the influence necessary to instigate such meetings, an alternative is to use the enterprise operating model visuals in enterprise IT governance meetings with the appropriate cross-functional leaders. For all requested changes, pose questions that foster a shared understanding of the options and trade-offs to be considered.

Success also depends on the CIO's leadership team. As a group, they must embrace the enterprise perspective, have strong business architecture and business design skills and strong process understanding (see "Toolkit: Business Architecture Presentation and Speaker Notes"). In mature IT organizations, the CIO's team leverages these competencies in combination with their design expertise, their motivation, and a vested interest in redesigning business operations and driving coherence across the enterprise. They use these competencies to bring business stakeholders together and help them make the right collective choices, deciding which trade-offs they can live with in pursuing digital ambitions.

Too often, realizing the enterprise ambition, such as a great customer experience, requires a set of integrated changes well beyond those requested by an individual stakeholder. These changes require time and money. Some of them could be done immediately or postponed. However, that choice has implications for how differentiated the "great" customer experience will be initially. Such a discussion will help the business stakeholders take ownership of the initiative and see that it is not simply an "IT project."

CIOs who do not seize the moment risk losing relevance at the business level and being relegated to "running the engine room." We predict that by 2021, CEOs will decide their CIO's career path; either as digital business transformation leader or as custodian of IT services that are shared. In mature organizations, we see enterprise architects joining business architects reporting into the business. Often, there is a demand for business design skills — designing the business and operating models — that isn't being fulfilled by the CIO's current enterprise architecture (EA) team. (Although this work is a natural part of EA, in many organizations, EA is often actually focused on enterprise technological architecture standards and solution architecture, not business architecture.)

CIOs can promote and lead enterprise operating model redesign by using the Gartner enterprise operating model framework to:

- Actively collaborate with the C-suite and enable the business architects to interact effectively with key business functional stakeholders.
- Move beyond the ideation phase of the digital journey and prioritize where to start.
- Use your team's design expertise (embedded in your business architects, your program leaders potentially and your developers) to manage complexity and demands for frequent change.

- Purposely lead the redesign of enterprise business operations to optimize resources and business capabilities.
- Drive coherence and consensus across the enterprise by influencing the design of domain-specific operating models.

This will establish the CIO as a business executive.

Digitalization is real and immediate. However, most enterprises are not executing effectively to achieve their digital ambitions. CIOs can leverage Gartner's business model and operating model frameworks as design tools for engaging with their leadership teams and partners. By working together using these visual aids, they can establish the right set of blueprints for their enterprise to create, deliver and capture new digital value at scale.

Research Highlights

This release of new business model research provides an overview of Gartner's enterprise operating model framework and offers guidance on how to position enterprise operating model innovation in relation to strategy and other management practices.

Here, we list other Gartner research that relates to our enterprise operating model research.

"Better Business by Design With the Business Architecture Landscape"

Leading organizations are transforming their business models to create new sources of revenue, services and experiences for customers. Enterprise architecture and technology innovation leaders must use a business architecture landscape to provide the insight and analysis required by senior leaders.

"A Detailed Examination of the Elements of the Business Architecture Landscape"

As organizations innovate to create new business and operating models, enterprise architects and technology innovation leaders can use the models of the business architecture landscape to make innovation possible.

"CIOs: Use a Grassroots Approach to Redesign the Enterprise Operating Model for Digital Business"

Enterprise business operations in most not-born-digital organizations will not sustain the pace of change, adaptability and scale required for digital business. A value-optimized information and technology operating model is key to executing digital business at scale.

"CIOs Should Use an Enterprise Operating Model to Improve Strategy Execution"

Clarity and effective processes are instrumental to executing strategy. CIOs should use the enterprise operating model as a tool to influence and improve strategy execution across the enterprise.

“Leverage Your Enterprise Operating Model to Shift From Efficiency to Adaptability”

Being able to adapt to hypercomplex market conditions is pushing leading enterprises to pursue radical new organization designs. To succeed, CIOs will need to understand how such changes impact the enterprise’s operating model.

“Why Business Models Matter for CIOs”

The mission of every enterprise is to create, deliver and capture value. Business models are a “blueprint” for accomplishing this mission. Digitalization brings new threats and opportunities. Top CIOs must master business models to define their ambitions and map their digital strategies.

“Creating Strategy at the Speed of Digital Business”

Creating strategy in a dynamic and rapidly changing digital world is challenging. CIOs should adopt an agile and iterative strategy process to enable the enterprise to respond quickly to new opportunities and threats and to keep pace with the speed of digital business.

“CIOs Must Leverage Both Business Models and Strategy”

Business model design and strategic planning play different but complementary roles in determining how a firm will compete, grow and prosper. CIOs who master and leverage both increase their executive influence and the perceived value of IT, while strengthening enterprise focus on what matters most.

“Combine Business Models, Strategy and I&T Operating Models to Understand the Scope of Business Change”

Enterprise strategy, business models and I&T operating models serve different and complementary roles. This research describes how CIOs can use these constructs to guide the coherent planning and execution of change.

“Maverick* Research: Operate Your Business Like a Lego Set to Win in Disruptive Times”

When the environment at a company changes rapidly, static operating models struggle to respond. Creating operational design agility with a modular operating model allows responsiveness to strategy and customer changes. (Maverick research exposes unconventional thinking and advice.)

“How to Choose the Right Type of Supply Chain Segmentation for Your Objectives”

Supply chain leaders rely on segmentation to enable growth, reduce costs and manage complexity. Unlike a maturity model, this research describes the different forms that segmentation takes within a supply chain and describes how to select the form suited for your desired business outcome.

“Strategic Benefits Realization: IT as an Engine for Coherent Execution of Strategy”

In this document, we introduce Strategic Benefits Realization, a Gartner methodology for increasing yields on investments in growth and transformation that involve IT.

"What Is an I&T Operating Model, and How Do You Accelerate Its Design Process?"

This research introduces Gartner's I&T operating model framework and a set of operating model patterns. CIOs can use this framework to accelerate the design process and provide a narrative for communicating the change.

"Run IT Like a Business by Applying the Service-Optimizing I&T Operating Model Pattern"

Digital demands have left IT departments run as a cost center disconnected from the business. CIOs should use the service-optimizing I&T operating model to run IT like a business, becoming a trusted partner with the credibility and influence to take on a proactive, consultative role.

"Monetize Your Business by Adopting the Value-Optimizing I&T Operating Model Pattern"

CIOs should adopt the Gartner value-optimizing I&T operating model pattern to play a proactive and essential role in achieving the enterprise's growth ambitions. Central to success is breaking down I&T and business silos, unlocking new value and resulting in a shift to business-outcome-derived KPIs.

Evidence

[1] See "Digital Business Transformation: A CIO Perspective."

[2] See "Use Business Capability Modeling to Drive Your Digital Business Design."

Note 1: Designing Independent Business Units

It is not just negligence that produces independent business units. Business units may run independently as a conscious executive decision to maximize market responsiveness versus economies of scale and scope.

Note 2: Business Capability Modeling

Business capability modeling is a well-established technique of enterprise architecture. When defining a future-state business architecture, the enterprise architect or business architect would use a somewhat different and more detailed approach. For more, see "8 Best Practices for Creating High-Impact Business Capability Models."

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