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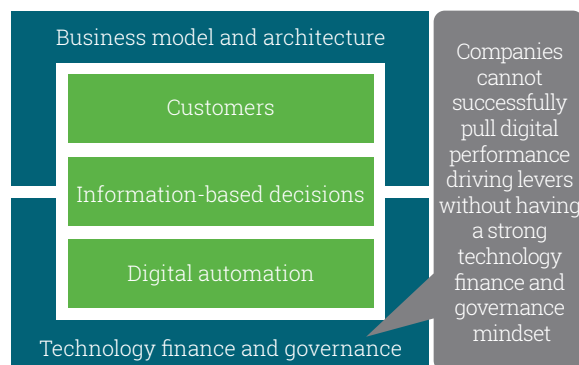
# Reimagine your IT spend as an investment portfolio

IT is a big spend category for any company—typically, 2 to 8% of revenue depending on the industry.<sup>1</sup> Many companies are starting to think differently about IT spending—particularly the top performers. That's because top-performing companies are generating returns from their overall technology investments.

To achieve such returns, you must stop running IT as a cost and think of it as an investment. You must run IT as a business, which requires an investment management approach combined with effective technology finance management practices. No longer will a one-size-fits-all IT investment strategy work. There are now multiple categories of IT spend to view based on a business's investment objectives.

Start including your IT experts in every decision you make. The governance of IT is equal in importance to IT's financial management. Most of the top-performing companies have highly integrated business and IT functions.

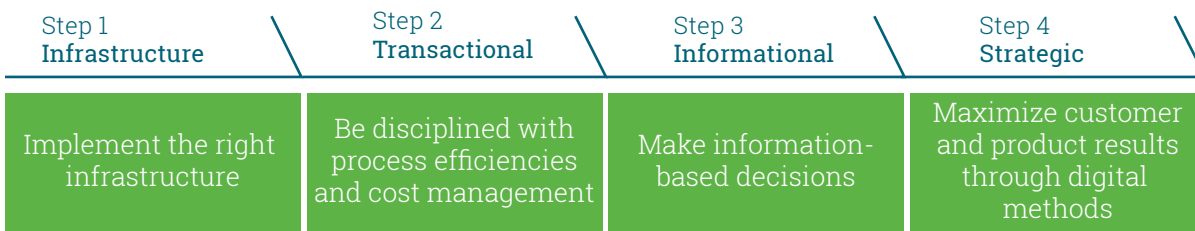
**FIGURE 1:** The digital transformation framework



Source: AlixPartners

<sup>1</sup> Gartner Group, *IT Key Metrics Data Report*, 2013.

**FIGURE 2:** Digital excellence progression across IT asset classes



Source: AlixPartners

### IT INVESTMENT ASSET CLASSES

Companies must make a mind-set shift in the way they think about IT—with regard to how they invest in it—along with acquiring the understanding that different business functions have different investment objectives. The following three functions provide a good starting point for that shift.

- **Running the business:** Managing basic routine transactions and functions and providing high quality at a lower cost
- **Improving the business:** Increasing operational profit, to be managed with the same rigor as any other business investment
- **Protecting the business:** Managing privacy and cybersecurity risk, spending just enough to comfortably manage risks

It can be a struggle to balance spend accordingly. Many of the finance executives we surveyed<sup>2</sup> responded that spending was weighted too heavily toward simply keeping the business running rather than toward improving it. Run and improve need to be interdependent, but cybersecurity should be handled separately based on a company's risk tolerance.

To help manage technology spend, it can be helpful to think of IT in asset classes that compose an investment portfolio. MIT's Center for Information Systems Research has established four categories of asset class.

- 1 Infrastructure services**, including servers, networks, and laptops, are accessed across the organization and used by multiple applications.
- 2 Transactional services** process routine business transactions with the aim of minimizing cost without affecting quality.
- 3 Informational services** provide reporting such as accounting, compliance, management information packets, and business intelligence.

- 4 Strategic services** gain competitive advantage by outsmarting competitors, understanding customers, enhancing products, and creating new business opportunities.

An effective sequence consisting of achieving digital excellence one step at a time is crucial as companies transform digitally (figure 2).

- 1** Implementation of the right **infrastructure** is a critical first step toward transforming digitally, but that implementation needs the right business model and the right enterprise architecture to share information, standardize processes, use shared services, and maintain a secure environment.
- 2 Transactional** investments standardize and automate basic business transaction processes (ordering supplies, billing customers, etc.) and with a focus on minimizing these investments, frees up funds for strategic investments. Costs are minimized by eliminating redundancies, instituting consistent, streamlined processes, and adopting machine-learning automation capable of performing standard tasks.
- 3 Informational** investments help better manage business rules to execute strategies based on real-time, critical information and to systematically direct frontline personnel to perform their functions and make decisions consistently and thoughtfully based on proper and timely evidence that supports those functions and those decisions.
- 4** High-performing companies execute **strategies** around enhancement of customer interaction and customer experiences as well as digitization of product features and maximization of their competitive positions by taking advantage of the confluence of recent technologies that provide abilities never possible before.

<sup>2</sup> CFO Research Services and AlixPartners, 2013. *Maximizing the Value of Information Technology: CFOs Dissect Their Companies' Spending and Return on IT.*

## **DIGITAL GOVERNANCE: BETTER TOGETHER**

The opportunities for digital transformation by fundamentally taking advantage and applying IT in support of your company's strategy have never been greater—or more challenging. You should consider how to lead your company in the right digital direction to support your business's goals.

Effective IT governance answers three questions.

- 1** What decisions should be made?
- 2** Who should make the decisions?
- 3** How will we make and monitor the decisions?

When it comes to IT decision making, business strategies and corresponding financial forecasts should be the driving factors; IT supports the execution of business strategy and helps the company meet or beat financial forecasts. For example, a company expanding into a new geographic region or acquiring another company needs IT to promptly establish infrastructure in the new region or support integration of the acquisition. Effective IT decisions cannot be made without knowledge of the business's primary strategies.

It is essential that technology decisions be made jointly by business and IT operations. Companies that have achieved both operational excellence and digital excellence and that have firmly integrated the two are realizing strong performance results and are IT savvy. Companies that are above average in both IT savviness and IT spending have margins 20% higher than their industry average. In contrast, companies with less than average spending and less than average savviness have margins 32% lower than their industry average.<sup>3</sup>

Technology projects should be prioritized and monitored by assigning benefit rating expectations and tracking realized benefits. Benefits ratings include quantitative measures of return on investment and qualitative factors with regard to how the project supports the company's strategies. Ratings are also assigned by combining project costs with the degrees of risk associated with the project's failure to meet expectations. Ratings are used for plotting each project on a decision matrix into low, medium, and high matrix segments and for reasons projects may be considered absolutely necessary, important, discretionary, or nice to have.

When decision making is in the wrong hands, prioritization and optimization of projects lag. Realistic cost estimates and benefit cases that deliver on business improvement objectives also suffer. Profitable companies do not give their IT departments the primary responsibility for prioritizing projects, but more than one-fifth of those reporting flat or down margins do so. Profitable companies are less likely to entrust to the IT department their business case documentation for improve-the-business projects and are much more likely to give that responsibility to sponsors from the business or functional units that would benefit from the projects.<sup>4</sup>

The growing integration between business operations and technological capabilities is causing the boundaries between business and IT to start to blur. Business and IT experts at the most-successful companies are speaking a common language; they have blends of business, financial, and technology expertise. Companies can develop those types of capabilities by transferring people between IT and the business units for cross-functional experiences and for the cross-training of business and IT personnel.

## **GE'S DIGITAL TRANSFORMATION**

General Electric Company is a prime example of an organization that is embracing the new digital world. The transformation of its business model is based on the belief that embedding software, data, and analytics into its products represents the future. Undertaking the industrial Internet initiative enables GE to provide tangible and measurable financial performance improvement benefits for its customers—so much so that GE is betting on those improvements through outcome-contingent pricing.

CEO Jeff Immelt has said GE is the oldest remaining company in the Dow Jones Industrial Average not because it is a perfect company but because it adapts. GE has a cultural history that has focused on winning through continuous learning and through sharing ideas about how to be more successful. That success-driven learning culture that constantly adapts is once again paving the way for successful change—this time through digital transformation.

GE's industrial Internet initiative serves to network with and connect everything in order to share information between machines, products, and people. Many sensors and data-collecting devices support GE's big machines such as jet engines, locomotives, and power plants to provide instant intelligence within the machines that is then used for monitoring, adapting, and improving performance.

<sup>3</sup> P. Weill and J. W. Ross, 2009. *IT savvy: What top executives must know to go from pain to gain*. Boston: Harvard Business Press.

<sup>4</sup> CFO Research Services and AlixPartners, 2013. *Maximizing the Value of Information Technology: CFOs Dissect Their Companies' Spending and Return on IT*.

GE's customers are realizing benefits from those revolutionary developments, resulting in the following industries saving billions of dollars.

- Oil & gas: Capital expenditure reductions in exploration and development
- Power: Gas-fired generation fuel savings
- Healthcare: System efficiencies
- Aviation: Commercial flight fuel savings
- Rail: Reductions in freight inefficiencies

As exciting as all of that is, it changes GE intensely across the entire organization. It's not just about changing the development of those products to include technology; it's also about how to bring the new concepts to market—and about everything else connected with them. All of this is creating whole new business models for GE as well as a new breed of large talent pool within GE that is different from the company's customary skill sets. The revolutionary developments have also created a new and additional set of competitors for GE such as IBM and SAP, which have similar technology offerings but not the physical products.

The new offerings require GE to be innovative and to customize its pricing whereby GE effectively aligns itself with customers and buys into the results. GE's new TenX Playbook guideline program makes sure that the value of the offerings is generating at least a 10 times return to its customer on the investment. GE has changed its offering philosophies from selling *products* to selling *business outcomes*.

The Internet of Things is starting to change everything in the industrial world. GE's culture and governance are conducive to accommodating that change and the company is reaping benefits from it. GE has been accomplishing the necessary business operations—technology integration by prioritizing the areas of its business that were more ready to collaborate. Other business areas within the company have seen that success and have had ideas shared with them. That sharing has been causing a domino effect of transition throughout the organization. As Chief Marketing Officer Beth Comstock said about the internal GE organization, "When you say, 'Look, this works,' it catches like wildfire."

GE has deployed governance tools to help the organization work across the changes that combine solution architecture with business capabilities to get the best results. Scorecards are used across the product development life cycle—from creating the idea to taking the completed solution to the customer. Quality is further bolstered through cross-functional training programs within GE.

GE believes that refusing to go in this direction is a mistake and that data-connected devices can radically distribute marketing power. If the company is right, it is destined for success, because it has the technology finance and governance mind-set to make it work. **A**

#### Sources for GE case study

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