

Tying the knot: IT integration in a merger

Two senior J. P. Morgan Chase executives, Thomas B. Ketchum and John W. Schmidlin, explain how a worldwide team set the stage for transforming the merged firm's IT organization

Brad Brown and Vikram Malhotra

The merger of Chase Manhattan and J. P. Morgan, in December 2000, created the second-largest US bank, with \$800 billion in assets. The formal announcement was just the starting gun in a race to mesh together the pieces and build a leading financial institution. Executives in every merger look to bring the results from consolidation to the bottom line. For managers at J. P. Morgan Chase, gloomy economic times made the pressure more intense.

Merging these institutions involved a massive effort to identify each heritage firm's "centers of excellence," to reduce complexity and inefficiency, and to reconcile different approaches to business. The two firms had thousands of employees as well as operations that spanned more than 50 countries. Chase was both a retail and a wholesale financial-services firm, Morgan a wholesale one. Their cultures, too, were distinct.

Bringing technology operations together effectively in a single entity was particularly crucial. Premerger technology costs were estimated at 10 to 15 percent of each bank's revenue, so tackling them would generate some of the largest cost savings in the deal. The cuts had to be managed very carefully, however—systems problems can be highly disruptive for companies that depend on technology to serve their clients. Moreover, the partners' separate technology organizations differed in some important ways, including procedures for managing costs and for choosing new IT investments. Finally, merging the two organizations was just the first step in a longer process aimed at establishing the building blocks of technological excellence.

Leadership of the overall merger effort was driven by a worldwide team of executives, including Thomas B. Ketchum, who before the merger had overseen technology,

operations, and finance as Morgan's CFO and chief administrative officer. By mid-2001, as integration plans were set and line-business leaders were taking responsibility for meeting their postmerger operating

Thomas B. Ketchum



EDUCATION

- Graduated 1972 with BA from Yale University

CAREER HIGHLIGHTS

- J. P. Morgan (1973–2000)
 - Management of various energy company relationships in United States, Europe; head of energy group in Europe (1973–84)
 - Various positions in Asia-Pacific, including head of region, excluding Japan (1984–87)
 - Head of Euroclear Operations Centre (1987–91)
 - Regional executive and head of investment banking for the Americas (1992–98)
 - Chief administrative officer (1998–2000)
 - Chief financial officer (2000)
- J. P. Morgan Chase (2001–03)
 - Vice chairman and member of executive committee
 - Chairman of technology council
 - Co-head of merger integration office and of productivity and quality program
 - Retirement scheduled for fall 2003

FAST FACTS

- Serves on board of directors for Zaplet, a private software company
- Member of development board, Yale University
- Member of President's Council on International Activities, Yale University

“Everyone sitting around the council table came with **great experience** and a point of view. But thanks to our governance structure, we were able to move discussions away from heritage models and people and to **focus on facts**”

targets, chairman and CEO William B. Harrison Jr. asked Ketchum to oversee IT, with two objectives: first, to ensure that the merger’s plans for technology were met and, second, to make technology a weapon of competitive differentiation.

To integrate applications development and infrastructure,

Ketchum quickly brought together his top team of technology executives from the two heritage organizations. The team also identified several critical information technology initiatives that would serve as the foundation for the longer-term goal of transforming IT.

To centralize and streamline the firm’s more than \$3 billion in IT infrastructure, Ketchum tapped an experienced former J. P. Morgan technology and operations executive, John W. Schmidlin. Over the next two years, J. P. Morgan Chase created a new IT infrastructure organization and achieved cost savings in excess of 15 percent. Schmidlin also led the firm’s groundbreaking \$5 billion, seven-year technology-outsourcing deal with IBM. The 2002 agreement calls for Big Blue to manage much of the organization’s IT infrastructure, including the data centers, distributed computing, and data networks.

In July 2003, Ketchum announced his retirement, and Schmidlin was named his successor. Schmidlin is now head of the firm’s technology

council and serves on the firm’s executive committee. The two men discussed their merger and IT transformation experiences in an interview conducted at the executive offices of J. P. Morgan Chase, in New York, with Brad Brown, a McKinsey principal, and Vikram Malhotra, a director, both from the New York office.

McKinsey on IT: Tom, what was your hypothesis about technology when you took over responsibility for it in 2001?

Thomas Ketchum: Our CEO, William Harrison, had asked the merger team to pay particular attention to technology because of the huge impact it has on our clients and because it was going to have the longest tail in achieving the merger’s benefits. In the very early stages of integration, we saw big savings, but we also saw well beyond that. Technology is an enormous competitive differentiator for any large financial-services firm. We had to lay the groundwork for a continuing IT transformation that would create a world-class function within a financial-services leader. The merger had created a firm with the scale, capital, and talent to do just that.

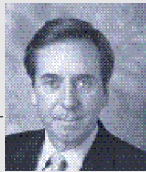
McKinsey on IT: Where did you begin?

Thomas Ketchum: We wanted to put together something new that wasn’t J. P. Morgan or Chase but was a combination of the best of both heritage firms. The immediate

John W. Schmidlin

EDUCATION

- Graduated 1969 with BS from St. John’s University
- Attended Cornell Executive Training Program in 1981



CAREER HIGHLIGHTS

- J. P. Morgan (1969–2000)
 - Management of various positions in the Stock Transfer Department
 - President of Morgan Shareholder Services Trust Company formed as wholly owned subsidiary of J. P. Morgan and Co. (1986–89)
 - Head of treasury operations (1989–90)
 - Head of foreign-exchange profit-improvement program (1990–91)
 - Head of technology and operations in Global Technology operations, Europe (1991–93)
 - Global business head of Securities Trust and Information Services (1993–97)
 - Head of global technology and operations for newly formed Asset Management Services (1997–2000)
 - Chief operating officer of Morgan OnLine, private-banking initiative; project manager of private-bank segmentation study (2000)
- J. P. Morgan Chase (2001–present)
 - Leader of infrastructure-delivery model initiative, which led to formation of Enterprise Technology Services
 - Chief technology officer of Enterprise Technology Services
 - Head of technology council and member of executive committee

challenge was to sort that out. In the first meeting of IT managers, who came from both firms, we saw clear similarities and differences in our operating models and in the basic economics for managing IT. So we started out taking an objective, fact-based look at the issues.

John Schmidlin: We also put a governance structure in place that brought our best technology people together and ensured that senior business executives would exercise oversight. On our technology council, each major line business was represented by a senior IT person. Several members of the firm's executive committee—the senior internal executive group—met regularly to review council issues, and a number of subcommittees, such as those for architecture and engineering, provided the council with specialized expertise. Everyone sitting around the council table came with great experience and a point of view. But thanks to our governance structure, we were able to move discussions away from heritage models and people and to focus on facts. The immediate cultural awakening was about costs. Smart people have a way of examining the facts and saying, “What are we going to do about this?”

McKinsey on IT: So you brought together a new governance structure. How did you and your team make important decisions about the merger?

Thomas Ketchum: We started working together very early on. For example, we had to make choices about a couple of thousand applications, to decide what was going to survive and what was not. We had to move fast, and we had to make sure any changes were completely transparent to our clients. Our approach may be a little unusual: we decided which applications to keep before we decided which technology people to put into place to manage them. We took a fact-based approach about the application functionality that best supported each business, and

“We took a fact-based approach about the application functionality that best supported each business, and we said that whoever was appointed as leader of a function had to implement these decisions”

we said that whoever was appointed as leader of a function had to implement these decisions. That created a lot of discomfort, as you can imagine. But it worked. Our transparency and objectivity gave us credibility with our peers, and successful execution established a track record for delivering on our promises. This created a foundation for us when we worked with business and IT leaders to make postmerger decisions, including centralizing the infrastructure.

McKinsey on IT: How did you use a similar approach in centralizing the organization's infrastructure?

John Schmidlin: We got everyone together and we focused on facts. It was very compelling to chief information officers and business executives to see opportunities for savings of greater than 15 percent. So then the discussion was, “If you buy this, you also have to buy into a new infrastructure governance framework and operating model,” which called for centralizing a lot of the technology infrastructure and defining new line-business interfaces into the infrastructure organization.

The combination of economic benefits, transparency, and a well-thought-out operating model convinced these people, along with the self-funding nature of our process—the opportunity to plow savings into investments for growth and innovation. We also talked with the executive committee members individually beforehand. As we started to centralize, we gave both technology and business leaders regular progress reports and communicated regularly with the entire IT staff.

Thomas Ketchum: As John says, there were two dimensions to the communications piece of that effort. For us it was about working out partner relationships with the senior management of the firm to make certain everyone was on the same page. But we also were very careful to communicate with our people, to tell them what was going on and why, and to admit that we didn't have all the answers but would continue to keep them updated as

could influence centrally. That was our model. The technology council would focus on big themes for change and on creating shareholder value. It would focus on critical firmwide programs—maybe three or four a year that we could work on as a group. Optimizing applications development was one of the four we identified during the merger. The other three were infrastructure streamlining, which included a

effective with the business. At the end of the day, the businesses are responsible for the end-to-end cost of their technology.

But that doesn't minimize the importance of the 20 percent owned by the council. Excellence in applications development is a multiyear, firmwide effort. Now that we've entered the transformation phase of IT, we are aiming at a lot more than cost savings—such as creating a simpler, more productive, better-managed environment; a stronger foundation to support innovation and growth; and greater clarity for our people on developing their careers. Behind those long-term goals are specific initiatives. They range from architecture standards and global-resource strategies, including the use of offshore talent, to fundamental improvements in our development processes, such as the use of Six Sigma and CMM and building a standardized tool set for managing the applications environment.

McKinsey on IT: You consolidated the IT infrastructure, cut its cost drastically, and then outsourced a significant portion of it to IBM. What did you seek to gain by outsourcing?

Thomas Ketchum: From the start, we made it clear to everyone that outsourcing wasn't just an expense-reduction effort. There were a number of things we wanted to get out of this. We set out a range of criteria and made them clear both to

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we figured things out. We were promising them that we would get the right people in a room and make decisions as fast as we could and be as fair as we possibly could. We wanted to make sure we weren't springing any surprises on our people.

McKinsey on IT: So you centralized the infrastructure. What about applications? How much centralized management went into this?

Thomas Ketchum: Very little. Our belief was that most of the strategy setting and execution for technology should reside in the businesses. We call it the 80/20 rule: 80 percent in the businesses and 20 percent we

revamped vendor-management program; strengthening our operational risk-management practices; and linking Six Sigma more tightly to automation.

McKinsey on IT: Is the 80/20 rule still useful to you now that the merger is complete?

Thomas Ketchum: Absolutely. Applications development is a good example of how that operates. We believed that applications development should be embedded in the line businesses—with the businesses accountable for it. Each of our line-business CIOs has undertaken systematic efforts to drive out costs and to become more

the vendors we were talking with and to our people internally. We said, “This is what we’re looking for, including world-class technical solutions, business resiliency, variable IT costs rather than the fixed costs of owning infrastructure, and access to the vendors’ IT talent and innovative ideas.” All those had to pan out. We had to have a much more comprehensive story to tell than just cost reductions. And I think that was well understood internally.

People were uncertain about outsourcing. It was a very big strategic decision. Some top managers of the firm reacted with skepticism. They said, “We already have scale ourselves, so why would we do this? The vendors have to make a profit, so after their margin how do we get serious cost reductions out of this? We lose control. There’s no turning back.” There were a lot of questions.

McKinsey on IT: How did you address them?

John Schmidlin: Just as we had earlier addressed the infrastructure-consolidation issues—get the facts on the table, do a lot of communicating, and rely on our track record in streamlining the infrastructure since the merger. We couldn’t have gone to outsourcing without the track record we had already compiled.

We were able to highlight a lot more than cost savings. We had established pricing transparency through a product and price guide

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for infrastructure services. This gave business managers a better idea of what they were paying for and helped us manage supply and demand for these services. We set up a vendor-management program that significantly reduced the number of vendors and lowered costs. And we set up a relationship program connecting our most senior IT people with our most important vendors. The program has turned out to be a great way to share ideas and to look for ways to make improvements. All of that gave senior management confidence in our ability to execute.

The vendors also helped us with the communications process. The CEOs and top people from both vendors that were finalists in our deliberations came in at least twice to meet with the executive committee to answer questions. The keys to this process were, again, the governance and operating model as well as our leadership team, which gave us the foundation that made the outsourcing decision possible. This was not just a technology decision but also a business decision.

Thomas Ketchum: Right. Another critical variable here was that we

went into the decision process with a clear sense of how much improvement we could do internally. In a lot of instances, as you know, companies decide to hand over a mess to a provider: “We’ll let the provider sort things out, and we’ll get 15 to 20 percent cost savings.” We didn’t do that. You leave money on the table that way. So we wanted to do our homework first. In the end, we had a very strong fact base for what we knew we could do ourselves, and we told vendors, “You have to beat this by a wide margin, not just overall but every year.”

McKinsey on IT: Who did the homework—IT or the businesses?

John Schmidlin: Both. The line businesses participated in the vendor assessments. We had teams looking at things like distributed computing, networking, and so on. The technology leaders representing the line businesses participated in the ratings of the vendor proposals and capabilities. Everyone was involved in assessing who was better in each category. The tech council was involved every single month. We kept the executive committee apprised of our progress, and it

provided input to the team. It took a year to reach a decision.

An important factor in this decision was how best to treat our people. We had people who would be let go as we became more efficient.

Outsourcing vendors like IBM, EDS, and CSC were in fact pulling people in—they needed people on the financial-services side. So we had 3,000 full-time people and 1,000 consultants who became employees of IBM, and IBM was delighted to gain the experience and skills of our people in one swoop.

McKinsey on IT: *How did you keep senior business leaders and executives involved? How did you get them comfortable with this?*

Thomas Ketchum: John personally spent an enormous amount of time gathering facts and then sat down with line- and corporate-business leaders to talk about the issues and

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listen to their concerns. It takes a lot of discussion to get people comfortable with a transformation of this nature. And they involved themselves. They’re smart businesspeople. They had a lot of questions and they asked them.

McKinsey on IT: *How do you maintain control over all of this now that you’ve given it over to an outsourcer?*

John Schmidlin: Several ways. We designed a governance model to deal with the new environment. We kept many of the old governance elements while adding new ones. New pieces of the structure included our inviting a senior executive from IBM to sit on our technology council as an insider with the CIOs from day one of the contract. The service-delivery representative from IBM sits on my management team in Enterprise Technology Services, which manages the IT infrastructure. We have a supplier-management board, made up of managers from IBM and managers from ETS, that meets monthly and monitors service. The final piece is an outsourcing-management board that includes Tom, three senior executives from the line businesses, and senior

members of IBM. They oversee the strategy of the deal. This is a multiyear transformation. We need alignment to solve problems and set the direction.

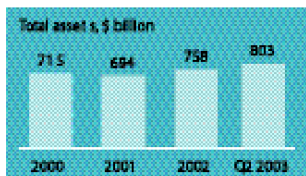
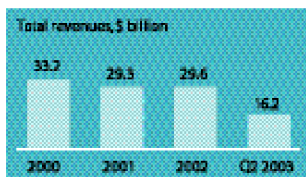
McKinsey on IT: *John, as the baton passes from Tom to you, one of the challenges you face will be to get even more mind share from the leaders of the line businesses. What other information technology challenges do you see coming in the years ahead?*

John Schmidlin: Business alignment and business accountability will be critical for us. As Tom has said, we’ve been shrinking the cost of IT, but we need to pay as much attention to the IT-investment side of the ledger: investments in business innovation, business impact. We must keep creating a capacity for innovation, things like on-demand computing and Web services. And when we make new investments, the businesses have to participate in those decisions and have accountability for them. Two years ago, we were focused on cutting expenses. But now we are directing our energy toward showing the economic business value of technology—technology’s added value.

The birth of a giant

J. P. Morgan Chase: Key facts

- + 93,000 employees (2003)
- + Operates in >50 countries, serves ~30 million consumers as well as corporate, institutional, government clients
- + Market capitalization = \$70 billion (Aug 2003)



Source: Hoovers, J. P. Morgan Chase; Morningstar; McKinsey analysis

That's one of the three challenges ahead of me. The second: we need to keep getting better and better about what we've put into place; that's operational excellence. You can't stand still. The third challenge is developing talented leaders and managers in IT. We need to create a new generation of technology leaders with broader, higher-impact roles. That will be a challenge for our leaders.

Thomas Ketchum: The technology council has been keeping track of a group of employees we call "corporate property." They are people with executive potential about 100 people. We see them as our top information technology leaders and want to help figure out where they ought to be going in the future. On the corporate level, our focus is clearly on the career development of our top leaders and on mobility. We

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do not have a mature process in place yet, but it is currently well under way.

John Schmidlin: Mobility helps to make the firm better and stronger because new people bring new ideas to the positions they hold. It instills a greater degree of objectivity in the organization because you are shaking up the inherent tendency of people to fall deeply in love with their own solutions.

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