

McKinsey on Business Technology

Innovations in IT management

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2 Five trends that will shape business technology in 2009

4 IT's unmet potential:

McKinsey Global Survey Results

14 Memo to the CEO:

Why we need an annual report for technology

20 How cloud computing challenges CIO roles:

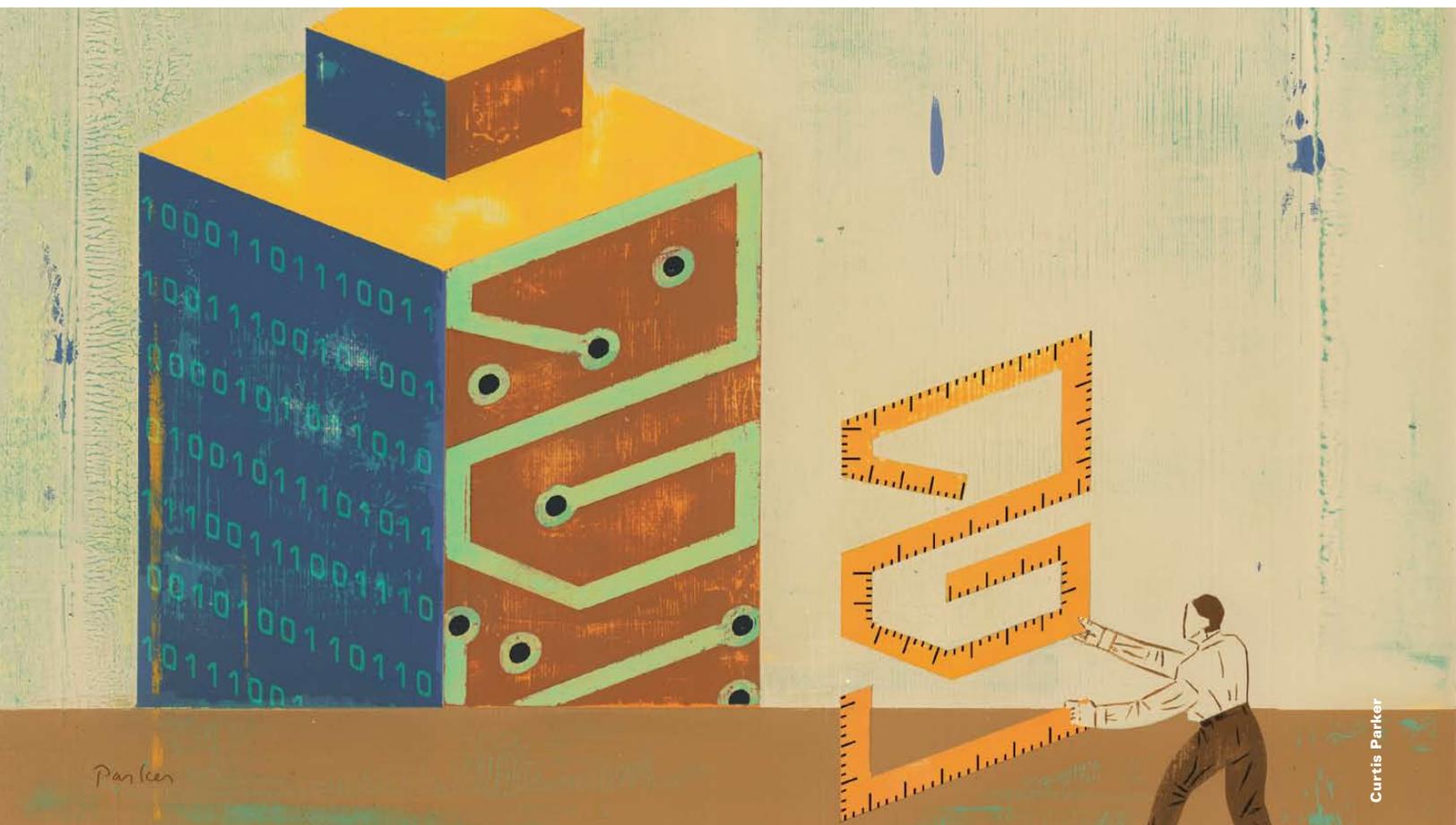
A roundtable

28 How CIOs should think about business value

38 Document management:

A hidden source of value





How CIOs should think about business value

Article at a glance

Many organizations can't get a true fix on the value information technology adds to the businesses it serves; defining, measuring, and maximizing that value remain elusive. To throw light on this crucial issue, McKinsey collaborated with CIGREF (the association of French CIOs) to study the best practices of a number of major French and international companies in various sectors. The key takeaway of this collaboration is a call for CIOs to broaden their scope of action by adopting new levers, roles, and governance practices that go beyond the purely technical and traditional IT capabilities.

Grasping the business value from IT is challenging. CIOs who are successful in this endeavor broaden their scope of action beyond the technical sphere and traditional IT levers.

**Michael Bloch and
Andres Hoyos-Gomez**

If there's any issue that routinely frustrates executives in many organizations, it's how to get a true fix on the value that information technology adds to the businesses it serves. IT is undoubtedly central to creating value and therefore continues to account for a rising share of total investment. But defining, measuring, and maximizing that value remain elusive. To throw light on this crucial issue, McKinsey collaborated with CIGREF¹ to study the best practices of major French and international companies across various sectors.²

¹ CIGREF, the "Club Informatique des Grandes Entreprises Françaises," founded in 1970, strives to "promote the use of information systems as a driver of value creation and a source of innovation." It includes more than a hundred public and private organizations from every economic sector in France.

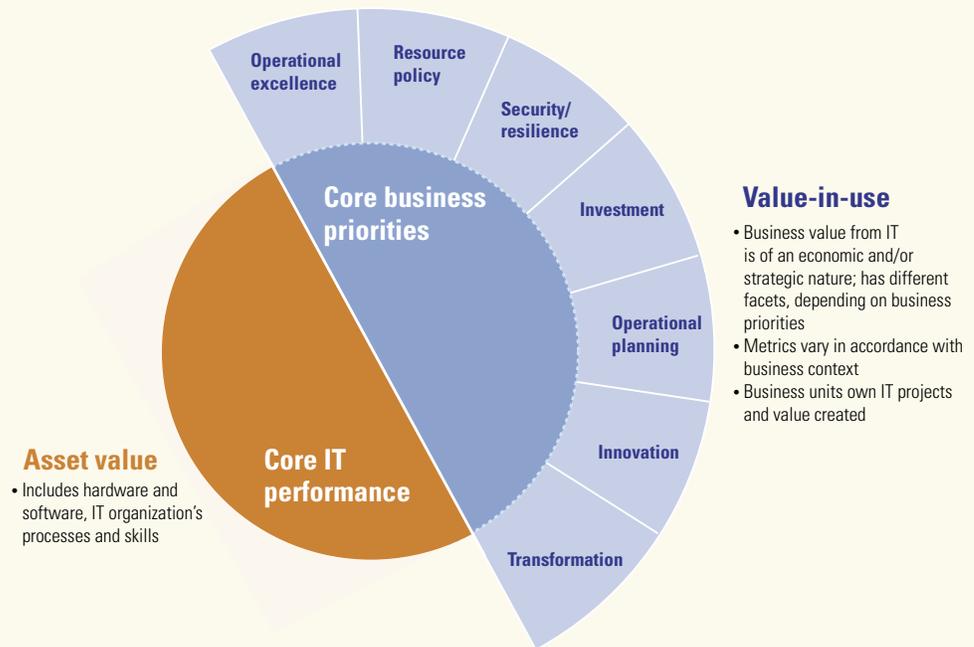
² "The dynamics of information-system-driven value creation," CIGREF and McKinsey & Company, 2008.

We interviewed 11 CIOs from these companies over a period from March 2007 to November 2007. The in-depth nature of these interviews provided valuable insights, as it allowed us to draw directly from the experiences of CIOs—many of whose companies have successfully used IT to gain competitive advantage. Analyzing their approaches to information technology helps to show how it can promote economic performance. We complemented these insights with international case examples.

Generating value-in-use

IT generates value at two complementary levels (Exhibit 1). The core asset value includes tangible items such as hardware and software, as well as softer benefits such as the IT organization’s processes and skills. IT’s vitally important value-in-use varies with a company’s core business priorities, such as whether it aims for an organizational transformation or operational excellence. A different set of metrics is needed to measure value-in-use, to account for both its economic and strategic dimension.

Exhibit 1
IT-generated value



Source: CIGREF; McKinsey analysis

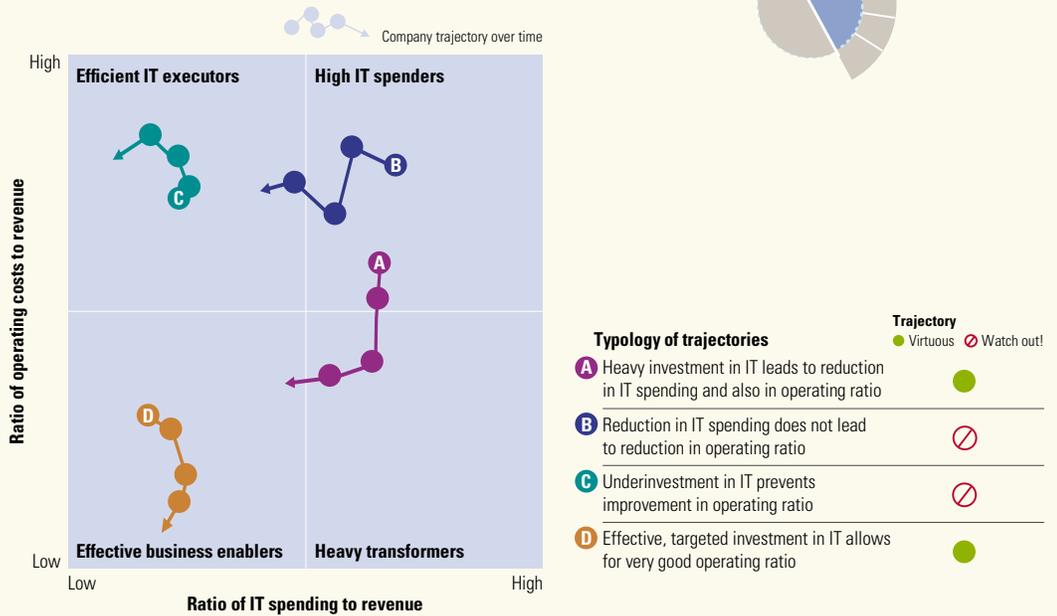
Optimizing investment value

Take the example of a group focused on optimizing investments among its various businesses—say, a banking group with multiple business units such as retail banking, consumer finance, capital markets, asset management, and the like. The economic value expected from the IT department can be measured through the improvement in the overall cost-to-revenue ratio, while the strategic value can translate into a competitive edge in terms of investment or acquisition capacity. (Since 80 to 90 percent of all synergies from banking mergers involve reducing the cost of operations, IT is indeed a key enabling factor during an acquisition.) The indicators that are tracked will be mainly financial, such as the ratio of IT spending to revenue, and will then be compared with the operating ratio—for example, operating costs over revenue (Exhibit 2).

Exhibit 2

Operating costs versus IT spending

Illustrative examples



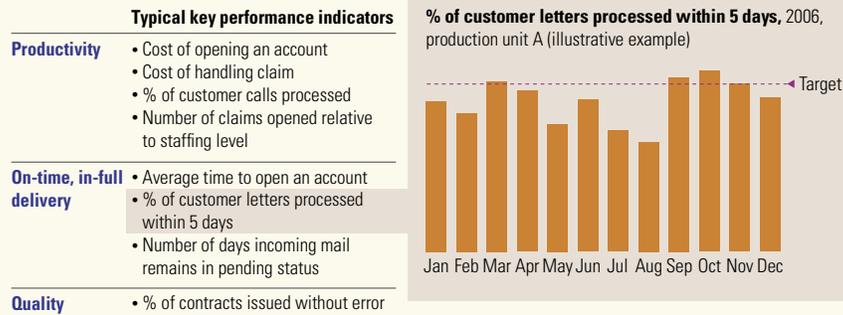
Source: CIGREF; McKinsey analysis

Measuring operations value

Similarly, in companies for which the priority is operational excellence (understood as quality and productivity of processes), the business value from IT will be measured in terms of key performance indicators (KPIs) at the process level. For example, IT will be seen as valuable if the systems helped to reduce the delay for processing an insurance claim or to ensure a no-error delivery of supplies to the production line (Exhibit 3).

At one global logistics company in our study, IT greatly improved supply chain operations—a key factor in a radical transformation—by helping the company to optimize its parcel-loading and truck-routing activities and to develop new value-added services, such as same-day delivery and made-to-order solutions for customers. IT also provided important data for more efficient risk management and better pricing.

Exhibit 3
Performance measures



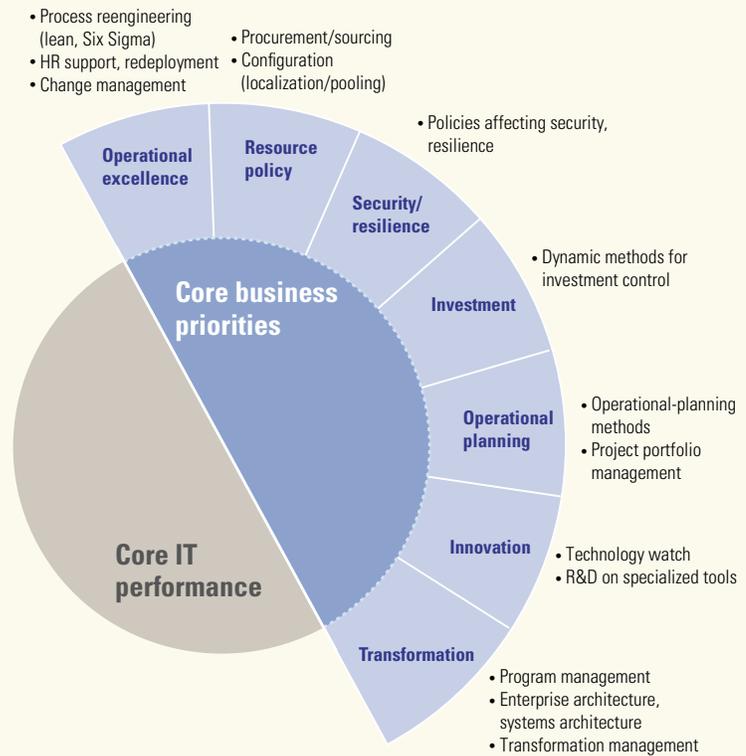
Source: CIGREF; McKinsey analysis



Finding levers where IT and business units intersect

Traditionally, a CIO’s main responsibility has been using standard practices and performance measures to maintain IT’s asset value. Developing value-in-use is a different ball game, however, and CIOs need to examine new levers found at points where the IT department and the business units intersect (Exhibit 4). To succeed, CIOs must take on new roles—bridging functional silos—that may take them beyond their comfort zones. For one thing, they will need to collaborate with executives in the business units to work on major transformation projects, to coordinate strategic planning, or to manage investments collaboratively (see sidebar, “Next steps: Identifying the challenges”).

Exhibit 4
Business performance through IT

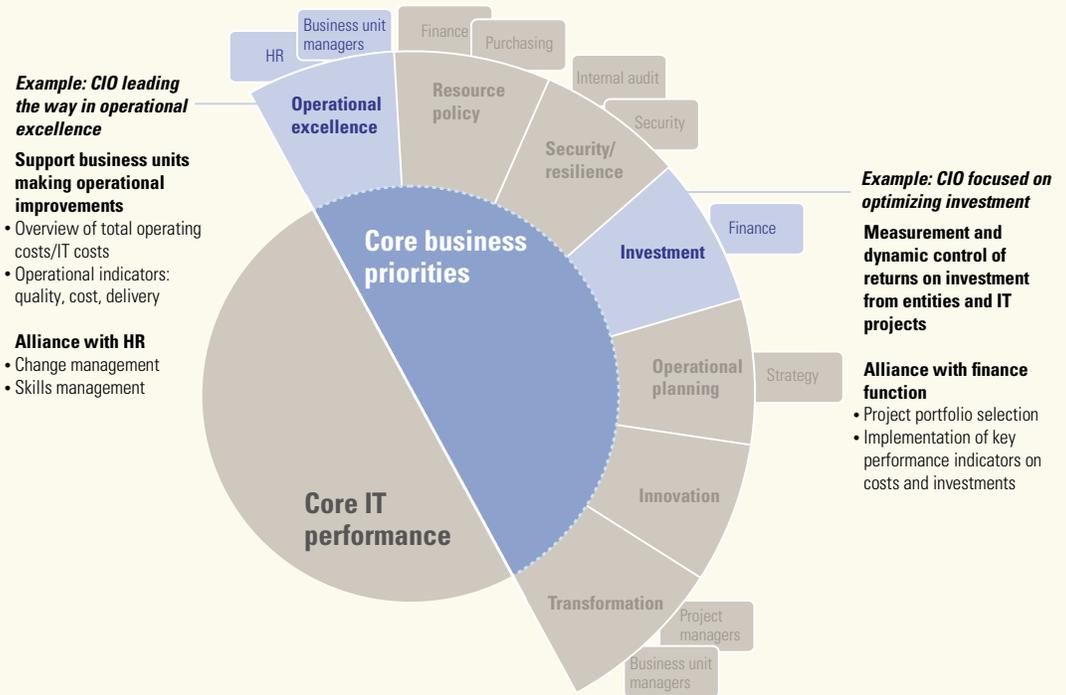


Source: CIGREF; McKinsey analysis

Seeking alliances

Cementing new alliances within the organization is critical (Exhibit 5). A CIO in charge of optimizing IT investments at the group level will need to assume responsibility for managing a portfolio of investments. To do so effectively, the CIO will have to join forces with the CFO, who has expertise in maximizing returns on investment. If the corporate goal is operational excellence, HR is more likely to be the CIO's preferred ally. This is due to the critical role of change management. Take the example of deploying a new enterprise-resource-planning (ERP) system: the critical challenge is ensuring that the target processes are codified correctly in the system, and that when it is implemented, the end users are sufficiently trained to effectively leverage the potential of the new tool. This requires a joint effort from HR and IT to synchronize and coordinate their tasks from the initial design to the rollout and subsequent life of the system.

Exhibit 5
Building alliances



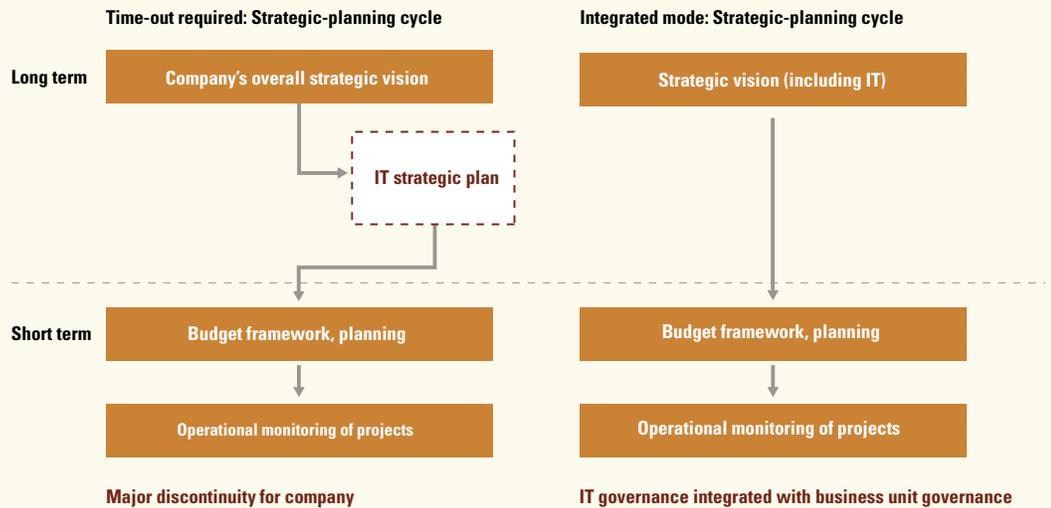
Source: CIGREF; McKinsey analysis

Building better governance

The businesses that are the best at creating value-in-use, we found, embed their IT governance within the broader governance practices. In practical terms, this requires IT representatives to participate in company forums that traditionally have been the exclusive domain of business unit leaders. At successful companies, certain core business processes, such as managing the business project portfolio or determining the allocation of resources, dovetail with IT processes. This notion of an integrated business-IT governance model can also apply the other way around: we have witnessed examples of companies where strategic planning for IT actually serves as a platform for broader strategic planning by establishing mixed business-IT forums (Exhibit 6).

Exhibit 6
IT-inclusive strategy

When a company faces a discontinuity (such as a business transformation or new kinds of market regulation), a strategic plan specifically for IT can help translate business priorities into IT initiatives.



Source: CIGREF; McKinsey analysis

Putting it all together

A simple framework summarizes the best practices we observed in our interviews. The value-in-use of information technology emerges when the IT department, building on a foundation of core performance, attacks problems and seeks solutions in areas that interest the business units and IT alike. Alliances with business leaders create new roles for CIOs and increase their scope of action. Governance practices that bring IT and business leaders together institutionalize this new way of operating.

Next steps: Identifying the challenges

At the best companies in our study, the CIO, the CEO, and the business units essentially cocreate value-in-use when they integrate the elements of our framework (Exhibit A). But to tap the potential reservoir of value, the new partners must have a clear view of the challenges they face (Exhibit B).

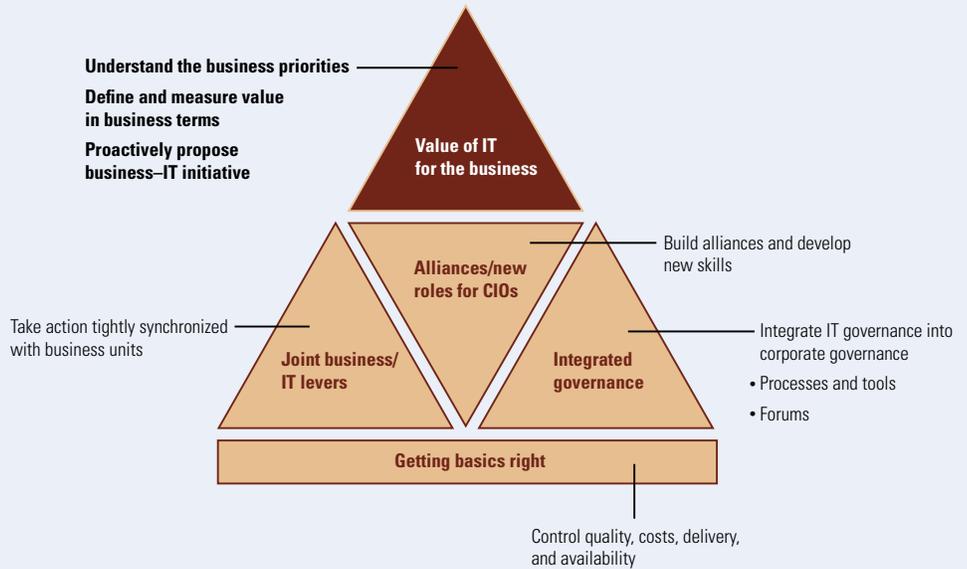
CIOs need to understand what the business units expect from the IT organization and to articulate IT goals in terms that business leaders can grasp. That means eschewing technology jargon, making innovative proposals, and taking firm positions on cross-functional projects. To be secure in these new roles, CIOs must develop a range of skills that transcend their IT core competencies; to give the emerging collaborative effort better grounding, they should create forums where IT and the business units can set common priorities.

For CEOs and business unit leaders, the main issue is mind-sets: they need to stop thinking of IT as a service provider and consider ways to build alliances with IT executives. IT priorities should be set in clear business terms. Leaders of businesses should proactively draw their IT counterparts into strategic and operational planning sessions.

When this approach works, it produces a range of benefits. Fresh synergies between IT and the business units create a wider palette of skills for both as they take ownership of shared projects and increase the intensity of their interactions. With leaders from the two groups finally reading from the same script, communications become more efficient, since less translation time elapses between the formulation of business plans and their execution by IT. Of course, the real bottom line is that these benefits combine to raise IT's value-in-use across the enterprise.

Exhibit A

Dynamics of value creation through IT



Source: CIGREF; McKinsey analysis

Exhibit B

Creating business value through IT: Benefits and challenges

	Benefits for company	Challenges	
		For CIOs	For CEOs/business units
Value 	<ul style="list-style-type: none"> Value-in-use of an economic and/or strategic nature for business units Business unit managers take ownership 	<ul style="list-style-type: none"> Understanding expectations about IT and formulating them in business terms Proactively proposing business-IT initiative Ensuring faultless execution 	<ul style="list-style-type: none"> Formulating objectives and priorities in business terms
Action levers 	<ul style="list-style-type: none"> A wider palette of IT and non-IT levers More effective levers 	<ul style="list-style-type: none"> Ranking priorities and sequencing levers to be used Taking a position on cross-functional projects 	<ul style="list-style-type: none"> Involving IT in cross-functional projects
Alliances and roles 	<ul style="list-style-type: none"> Pulling IT and business unit skills together and fitting them to the context 	<ul style="list-style-type: none"> Developing non-IT skills Being collaborative Reinforcing IT's cross-functionality 	<ul style="list-style-type: none"> Moving the CIO away from a purely technical focus
Governance 	<ul style="list-style-type: none"> More direct interaction <ul style="list-style-type: none"> No translation phase More business-centered dialogue 	<ul style="list-style-type: none"> Creating symbiosis between business unit forums and IT forums 	<ul style="list-style-type: none"> Bringing IT into strategic and operational planning for business units

Source: CIGREF; McKinsey analysis