

# Making IT pay

COMPANIES RARELY CALCULATE THE VALUE THEY REAP FROM WHAT THEY SPEND ON INFORMATION TECHNOLOGY BY BRAD HOWARTH



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DAVID MURRAY: Looks for quick results and returns

**A**ustralian companies spent \$23.7 billion last year on information technology (IT) — and most of them had only a vague idea of why. Despite decades of investing in IT, most companies cannot say whether the investment has helped to increase shareholder value. IT industry analysts say most companies accept that they cannot do business without IT, but few have accurate systems for measuring the return on their investment in it.

The consulting firm DMR Consulting has been helping companies understand the value of their IT investments for the past decade. DMR Consulting's director, Dave MacKenzie, says problems with understanding and measuring value have become a big issue for senior executives as tight economic conditions, increased competition and greater complexity in their organisations have

forced companies to analyse their investment decisions more carefully.

"I haven't met a chief executive yet who does not agree with the pressing need to better manage the realisation of business value from their IT investment programs," MacKenzie says. "In most organisations, the fundamental issue of extracting business value out of their IT investments is not actively managed." He believes, too, that most companies focus on their ability to use technology, rather than on the value the technology delivers to the business.

MacKenzie says: "The Meta Group [an analyst company] estimates that effective portfolio management of investment programs can reduce costs by 30–40%, so there is plenty of upside to understanding and managing the value of IT investments. If there is not some systematic change, business leadership will continue to be frustrated by an unacceptable level of under-performing programs, lost opportunities from great ideas that did not generate the interest

needed to get started, and, perhaps most importantly, the long-term erosion of key assets, such as quality staff."

The Asia-Pacific senior vice-president at the research company Gartner, Bob Hayward, says: "Companies that fail to understand the value of IT either run the risk of not taking advantage of IT innovation to drive growth and reduce costs within their organisation, or they indulge in excessive investment, much to the delight of suppliers but at a great cost to the enterprise."

Studies conducted by the research company IDC Australia show that, since 1996, more than 60% of business executives believe IT contributes to operational effectiveness. But the proportion of executives who have been disappointed with the return from an investment in IT has climbed from 1.5% in 1996 to 3.3% this year. More importantly, the proportion who believe it has given their company a competitive advantage has fallen from 21.9% to 16.3% over the same period.

Although some companies struggle to establish the return on investing in IT, a report released by the Organisation for Economic Co-operation and Development (OECD) in October last year found that investment by business in information and communication technology (ICT) between 1995 and 2000 lifted the gross domestic product of Australia by 0.68 percentage points a year. Only the United States had a bigger increase, of 0.87% percentage points.

John Rimmer, the chief executive of the Federal Government's IT policy group, the National Office for the Information Economy, says investment in IT has had a favorable influence on the Australian economy, but not as much as some people believe. One reason the impact is not as big as thought is that the OECD report bundles together all the good investments in IT and all the bad investments, he says. Hence, the net amount of benefit is smaller.

"In some sectors of the economy, we have been incredibly effective users of IT. Mining and financial services are standout examples and, increasingly, agriculture as well. There are other sectors where there are a lot more obstacles. Transport and health are two examples."

The executive chairman of the business information company IBISWorld, Phil Ruthven, says there are other indicators that technology has had a favorable effect on Australian business. "The profitability of our major corporations has been creeping up at a rate of about half a percentage point a year — we were earning about 9% [profit as a percentage of revenue] in the 1990s, but we are heading up to 13%," he says. "We are creeping up the scale of international competitiveness, and our bottom-line results for major companies are creeping up, some of which you could put down to our high adoption of ICT by world standards."

Investing in IT might have made Australia more productive and competitive, but in the past two years there has been a backlash against IT investment in some companies. In February, David Murray, the managing director of Commonwealth Bank, blasted the IT industry at a conference, criticising it for over-promising and under-delivering, and claiming that any productivity gains the technology industry may have made were wiped out in the April 2000 tech wreck.

Murray says he is aware of the importance of IT to Commonwealth Bank, but used his speech to stress that the competitive nature of the IT industry can lead people to forget the realities of doing business, and that the adoption of technology for the sake of it is not a good business strategy. He says that just as

## The traps

Lessons from information technology projects:

- A commitment to measuring the value of an information technology (IT) project needs to begin when the project begins. If a system to determine return on investment is not in place at the start, the ability to determine the return when the project is completed is reduced.
- Many IT departments have been allowed to operate independently of the business they serve, with different objectives.
- IT projects can often span several years, during which time the company's requirements or circumstances might change significantly. Such changes can affect the scope and success or failure of the IT project. Staff can also leave during projects, taking vital knowledge and skills with them.

SOURCE: BRW

PAUL JONES



some suppliers oversell the benefits of technology, so do some buyers overestimate the benefits.

Murray says Commonwealth Bank has a rigorous evaluation process for each new IT project. The bank has moved away from large-scale implementation and now breaks IT projects into smaller components that can produce results, and returns, more quickly.

"The danger is always there with any new piece of technology, that, if I don't adopt it, one of my competitors will, and will gain a competitive advantage," Murray says. "We are not technology developers and we are not creating patents as such, so I suppose everything we do is based on knowledge that someone else could know. What we can do is adopt early and use it well to build an advantage with customers."

He points to Commonwealth Bank's online banking system, NetBank, which was launched in February 1997, as an example of how the early adoption of technology can produce a competitive advantage. "We decided early on that our customers would want to do banking online, so we built that service, which now has 1.5 million customers," Murray says.

Initiatives such as NetBank and Commonwealth Securities, the bank's online share trading division, "introduce risk" by placing big demands on the bank's IT systems and its ability to provide services. But Murray says that embracing new technology has given the bank a lead over its rivals.

In general terms, IT projects fall into two categories: projects that produce cost savings and efficiency gains, and those that increase sales. Last year, many companies responded to difficult economic conditions by using IT projects designed to cut costs. Joel Martin, a director of IDC Australia, says the main value of IT has been in



**FIONA BALFOUR:** Staff are keenly aware of the need to consider benefits

of 6-7¢ per garment. "If you handle a million garments, it's quite a lot of money," he says.

At Suncorp Metway Bank, the group executive in charge of IT, Carmel Gray, says a rigorous investment governance process has been introduced to assess the merit of all IT investment requests submitted by business units. A committee consisting of Gray and the bank's group executive for corporate projects and chief financial officer reviews each request.

Since its merger with GIO in June 2001, Suncorp Metway has embarked on a business transformation program consisting of more than 790 projects. The program includes roughly 120 IT projects, which are expected to achieve \$240 million in cost savings by 2003. Gray says most decisions on IT investments are based on the level of commercial benefit that flows from them, although some are more strategic and are designed to maintain or improve the bank's brand or reputation. "Our view is that every project should stand on its own feet from a return-on-investment basis," Gray says.

How well IT investments are tracked within an organisation often depends on how closely IT is aligned with the goals of the business. In many companies, the IT

department has been allowed to distance itself from the rest of the business, particularly where IT executives have had a poor understanding of business, or business executives have had a poor understanding of IT.

helping companies to re-deploy and reduce staff by eliminating unproductive work and by making processes more efficient.

"[IT investment] is replacing paper processes," Martin says. "It's not changing the way we do business, it's reducing the paper trail."

Murray says many IT investments made by Commonwealth Bank since the late 1990s have been designed to cut costs and make processes more efficient. "Over the past five years we have made consistent reductions in our banking margin as a result of improved efficiency," Murray says, "but there is no point in doing something that creates a new efficiency if the customers cannot come with us. We cannot mandate a change in customer behavior."

Hayward says it is impossible to draw a direct link between a successful company and a strong IT strategy. "Real business success is more to do with strategic decisions made on mergers and acquisitions, products and services," he says. "IT is an enabling technology that supports a business strategy. If the business strategy is wrong, it does not matter how much you are investing in technology, you are going to fail."

IT can provide the impetus for business growth. The managing director of the women's clothing retailer Noni B, Alan Kindl, says he would not be able to operate the company's network of 140 stores without IT infrastructure. Noni B set up its first retail system in 1979, and now runs a range of systems from the local software developer Retail Directions.

Kindl says technology enables him to see which goods are selling well or poorly in which stores, and move stock around accordingly. "You wouldn't exist without IT; you would have no idea who is selling what," he says. Kindl says a recent upgrade of Noni B's warehouse system increased its efficiency by 25%, the equivalent

of 6-7¢ per garment. "If you handle a million garments, it's quite a lot of money," he says.

Gartner's Hayward says that chief information officers (CIOs) who do not articulate the value of IT within their company run the risk of losing credibility. "CIOs may assume their efforts are appreciated and are providing real value, but the reality can be very different. Credibility is the main aim of most CIOs and is a currency whose worth should never be underestimated. Once credibility is lost, the CIO's job becomes far harder — every expenditure and initiative is minutely scrutinised, morale plummets, people leave. Every effort is put into fire-fighting instead of building a real fusion of IT and business strategy, based on common perceptions of value."

The CIO at Qantas, Fiona Balfour, says that, for the past 20 years, the people who have run the airline's IT department have had general business — rather than IT — backgrounds. "That makes an enormous difference in how IT is seen inside the organisation, and also at the executive table," she says. "We are part of the business."

Balfour says Qantas has developed formal methods for tracking the value of IT. "We write the budget benefits of IT projects into forward-year projects for each business unit, so that makes people keenly aware that when they put ideas forward they have to take the benefits of investments into account. The corporate governance of how we spend our IT dollar is almost institutionalised, and we have very formal instruments to maintain that." ●