

# Bulletin

## Driving to success

### How IT in financial services requires the skills of a Formula One team

The average driver looks out at the road ahead, with an occasional glance at the dashboard and the rear view mirror. Notwithstanding the usual distractions of cell phones, hot coffee and XM radio, most drivers arrive at their destinations safely. Consider a Formula One race car driver. In addition to moving at upwards of 200 mph, he (or she) must contend with over 40 read-outs from on-board computers covering speed, angle into the turn, gear shift, brake pressure and other indicators for optimizing performance. In both cases someone is driving a car, but with significant differences in objectives, G-force, and the amount and velocity of information to be processed.

The metaphor aptly describes the management challenge in information technology today. Strategic management of IT, particularly in Financial Services, is about understanding what business information matters, the velocity of change, and what to do about it . . . while you are driving. Product profitability, customer preferences, capital optimization, credit exposure, et al., are the dials on the dashboard. If you are an average driver, you may not know what all the dials are for, or how they work in concert to tell the performance story. Conversely, trying to operate a vehicle with your eyes glued to the controls is also a bad idea. The trick is having the right combination of information available for the problem or mission at hand; this implies the ability to read and respond quickly to a fast-changing environment (see exhibit 1).

Most business executives are aware of this IT dilemma: too much information chasing too few real uses. What they don't universally seem to know is what to do about it.

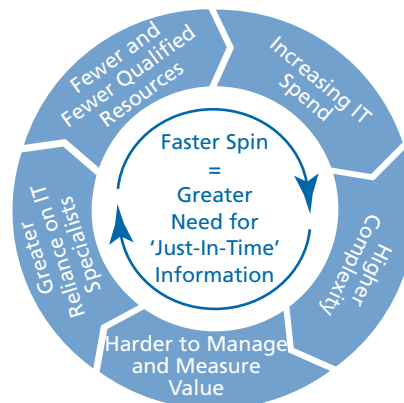
Why not?

First, because it is diabolically hard to measure the value IT spending creates. Most businesses still look at IT in terms of cost or headcount, not at what it means for shareholder value. If a bank with a market capitalization of \$40

 MARSH ER EP  
GUY CARPENTER WYMAN

BN spends \$2 BN a year on IT, is that good or bad? Is that level of spending a competitive necessity or delivering a strategic edge? How does the \$2 BN expenditure contribute to the firm's market value? Possibly not at all—if, as

Exhibit 1. Information velocity and the IT dilemma



the research suggests, the savings IT delivers are realized by productivity gains shared with customers and the rest of industry. On the other hand, IT may be contributing to the nth degree, since without this spend the bank would be unable to operate or even keep up with the competition. Either way, this example illustrates that management needs to think carefully about how to demonstrate the value of its IT investments to the market through increased transparency, agility and business performance.

A second problem is that IT is not a monolithic, lump-sum expenditure, but a highly diverse set of services —some of which are completely intertwined with and indistinguishable from the business, others of which are more like utilities. Lumping all these types of IT spend together for investment and management purposes is a mistake, albeit one made by many firms. Executives should differentiate dollars spent on new competitive capabilities versus investments in commodity infrastructure.

IT represents at least four distinct services or capabilities:

- Core capabilities embedded in business operations and therefore practically indistinguishable from the business which they support (e.g., loan origination or loan accounting systems)
- Infrastructure needed to deploy the business function in a timely, cost-effective manner (e.g., middleware and MIS reporting), typically across multiple lines of business
- Commodity services on behalf of the enterprise as a whole, not that different from other utility functions such as facilities (e.g., telecommunications, desktop PCs)
- Management and processes which provide the structure and administration around deployed capabilities (e.g., architecture, planning, support).

Each IT capability has a different value proposition, management philosophy (e.g., service quality versus cost) and range of options available (e.g., build or buy, outsource or insource). To be effective, IT spending must be aligned with the business capability provided; IT cannot be viewed merely as a cost to be managed down. Understanding these distinctions is essential to managing IT assets effectively and making the right choices.

Third, senior management should recognize that more than half of IT costs may be hidden —either because they are embedded in the business and

therefore not under central control, or because they are wrapped up in the intractable complexity of the systems themselves—and if senior managers can't see the IT spend, they can't control it. Most financial institutions suffer from excess complexity in their systems environment—a problem that's been compounded by the never-ending mergers in the industry as well as years of modifications. Introducing new business functionality while keeping old systems running is an expensive proposition. Unraveling 'good' (value as a result of variety) from 'bad' (unwarranted) complexity places a premium on R&D, architecture and measurement. Management would do well to incorporate new ways of thinking about IT complexity—comparing both the real and hidden costs as well as evaluating the risks of sticking with complex legacy systems versus moving to more capable platforms.

### Applying a business lens to IT

'You can't manage what you don't measure' is the old adage, one that particularly resonates with IT. The challenge is how to express the results of IT investments and activities in terms of tangible business outcomes. Companies like Dell, Wal-Mart and other retailers concluded a decade ago that front-to-back information management was not just a function of doing business but the basis for their business model itself. Their CEOs rallied the organizations around themes like reduced carrying costs, negative days of inventory and just-in-time assembly. By expressing the performance of IT in measures of business value, executives produce a much more transparent vision of IT impact.

Exhibit 2. Applying a business lens to IT

| IT Management Principle                   | Business Management Analog                                  |
|---|---|
| Measurement/management by objectives      | KSFs, KPIs, PBOs, P&L, balanced scorecard, financial ratios |
| Framework for investment decisions        | Strategic and operating plans, capital plans                |
| IT talent management and development      | Professional development/ succession planning               |
| Technology visioning and 'real' options   | R&D; venture capital  |
| IT portfolio balancing and alignment      | Portfolio management; decision theory                       |
| PMI-IT; technology selection and adoption | M&A due diligence, business cases                           |

At Oliver Wyman, we believe the hallmarks of better IT management are found in solid business management concepts (see exhibit 2):

- *IT investment decisions* should be made in the context of how well new initiatives fulfill and deliver business priorities for the whole firm. Requires portfolio-level assessment of scope and resources up-front, and delivery backed by management prepared to intervene to ensure success
- *Talent management/development* that recognizes IT expertise as a corporate asset, especially in the current climate where we have rapid change, a shortage of high-end skills and an issue with retention. Requires a focus on priority skills to deliver business objectives (e.g., business analysis, operational risk)
- *Technology options* where traditional valuation approaches, such as ROI, are no longer meaningful (e.g., IT investments to exploit uncertain

market opportunities). Requires strategic hedging mindset to position the organization for rapid exploitation or exit of technologies as they mature

- *IT portfolio re-balancing and alignment* to focus technology investments, highlight tradeoffs and ensure explicit choices. Requires 1)effective forum for business/IT dialogue; 2)process for prioritizing technology investments; and 3)process to break ties and promote LOB synergies.

Today's business environment is one of increasing information velocity, which makes most in-house IT platforms more—not less—critical and strategic. At the same time, managers want better information on customers, capital and risk with greater accuracy, granularity and frequency. But are they asking the right questions?

At a minimum, senior business executives should ask themselves and their CIOs the following:

- Do you have a good way to measure IT performance across service, cost, productivity and innovation dimensions? Do you ever go back and evaluate how you did against these after the fact?
- How are IT investment decisions made? Against an agreed business architecture? Prioritized against a portfolio according to business impact? With or without real business cases?
- Do you know your organization's critical IT skills? How do you source, retain and develop them?
- What technology bets should you be placing, and when? How much should you wager? What is the right mix of short-term and long-term bets?
- Do you know what your highest value IT projects are? How do they further your business aims? What structures and processes are in place for managing them?
- How complex is your systems environment? How much of a cost penalty (premium) are you running? How exposed are you with or without technology renewal? How will you determine whether you are receiving value?

Answers to these, be they only partial, should help make Formula One drivers out of even the most technology-wary executives.

## OLIVER WYMAN

For further information please contact

In North America  
1 212 541 8100  
marketingna@oliverwyman.com

In Europe  
44 20 7333 8333  
marketingeu@oliverwyman.com

In Asia Pacific  
65 6510 9700  
marketingasia@oliverwyman.com

Copyright © 2005-2007 Oliver Wyman

All rights reserved.



MARSH MERCER KROLL  
GUY CARPENTER OLIVER WYMAN