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Info you can use:

- Avoiding risk by using technology to drive competitive advantage
- Reactive and proactive risk management strategies
- Viewing information technology organizations in terms of business value
- Extending your business technology horizon beyond Y2K
- A focus on real-world enablement, as opposed to emerging possibilities

DISASTER

TECHNOLOGY'S ROLE IN RISK MANAGEMENT

By Ray Arpin, META Group

If you think that you have averted disaster because your Year 2000 (Y2K), euro currency, and even technology infrastructure issues are under control, think again.

Fixing one problem may be causing others that aren't even on your radar screen yet. Such is risk. The real question is this: Are you focused on the right things at the right time for the right people? Many IT/IS (information technology/systems) organizations are facing significant hurdles in demonstrating their contribution to the business. They are just now realizing that they may not be focused on the root cause of the problem, and that they don't know what to do about it. However, a few leading companies have recognized a new focus—value—along with a need to identify, define, quantify, and measure the value of IT to the business.

To put it mildly, this is no simple task.

Muddy Waters

Business complexities are increasing with the number of mergers and acquisitions across industries. Meanwhile, the rapid growth of Web-based commerce is becoming a competitive driver for customer mind share. Each of these issues requires strategic planning and IT integration with the business. Dealing with more than one issue at a time, which is currently occurring in most organizations, requires the implementation of a basic "value approach."

Risk management and contingency planning have also become hot issues, especially as Y2K approaches. As a result, more business people are demanding that the IT organization justify spending, add value to the company, and enable a competitive market position. This further increases the importance of risk management and contingency planning and requires taking IT beyond total cost of ownership issues—or cutting it to the bone.

The question organizations should be asking themselves (and the leading ones are) is this: How do we get from cost-based to value-based thinking? Merely focusing on cost causes a downward spiral that results in diminished core competencies, knowledge, and intellectual assets. Focusing on value leads to the creation of a framework that both IT groups and business units can understand—especially when value is defined as the sum total of future benefits to be realized.

With business disciplines shifting to new paradigms, IT strategies and departments can be viewed as either laggards or leaders. The question

PROGRAMS INVOLVING TOTAL COST OF OWNERSHIP, COST REDUCTION, AND BUDGET SLASHING ARE CAUSING PROBLEMS FOR MANY ORGANIZATIONS. THEY FOCUS ON CUTTING COST, BUT THEY CAN LEAD TO LOSS OF VALUE IN TERMS OF BUSINESS CAPABILITIES, INTELLECTUAL CAPITAL, AND HUMAN RESOURCES.

that CEOs and stakeholders are now asking is this: What value does IT provide to the business? As business economics and markets change, so too must the view of IT. The bottom line is that IT strategies and investments cannot be optimized without a value approach. Therefore, leading IT organizations are beginning to ask how IT:

- Increases revenue
- Improves productivity
- Reduces cycle time
- Mitigates risk

Indeed, risk is just one element in the valuation of IT to the business.

Risk Management

So just what have we learned from the Y2K dilemma? Many IT organizations have realized that they have simply been reactive, and some are moving to become more proactive in terms of business planning, because solving one problem at a time in a reactive manner can create other, even larger, problems. The solution is to consider all business elements as part of your IT strategy.

Approaching the problem in this manner definitely requires a risk management program—just make certain it is applied in the context of value to the business as a whole. However, you should realize that most risk programs typically look at what-if scenarios, which are reactive by nature and, thus, propagate many companies’ current IT problem-solving paradigms.

Scenarios that have been identified as potential sources of concern in risk management programs include:

- Year 2000
- Euro currency
- Major enterprise resource planning (ERP) initiatives
- Market and business paradigm shifts
- Globalization
- International crises and political instability
- Security issues

Conversely, a value management focus can be proactive and looks at the contribution of IT to the business. The key element of this focus is that IT considers all critical business needs which, if not addressed, add to risk itself.

Another strategy employed to reduce risk is simply to cut costs. Programs involving total cost of ownership, cost reduction, and budget slashing are causing major problems for many organizations. These programs focus on cutting cost; however, they can lead

to loss of value in terms of business capabilities, intellectual capital, and human resources. As one IT manager said, “Cutting the fat has led to cutting into the muscle of the organization, almost to the bone. We have lost more than we will ever get back.”

What is needed is a way to consider IT investments as business enablers and value contributors—something we refer to as the CIO Value Initiative (see graphic).

Value Management

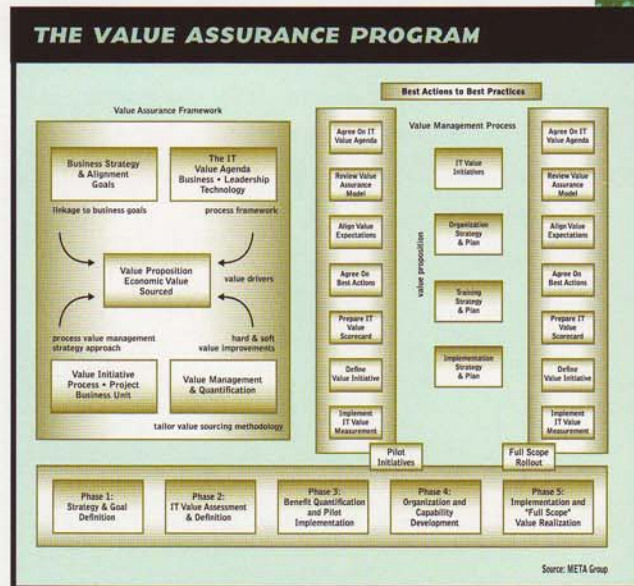
Questions that CEOs, shareholders, and stakeholders are asking involve looking at how IT contributes to the business. Some of these questions are:

- What is our position, and how did we get here?
- What are we going to do, and what will it cost?
- When does it need to be done?
- Who is responsible for results?
- What are we going to do to make sure it doesn’t happen again?
- And especially—what value does IS/IT bring to the company?

Fundamentally, this is a value measurement problem. Our research indicates that two disturbing facts impact an organization’s IT effectiveness:

1. Companies that do not measure the value of IT typically manage IT as a cost center and continually cut spending.
2. Only 5 percent of companies have any value measurement systems for IT.

The overall problem for most organizations is



SOME PREDICTIONS SAY THAT 10 PERCENT OF COMPANIES WILL FAIL DUE TO Y2K PROBLEMS. ANOTHER ESTIMATES THAT 10 PERCENT MORE WILL FAIL AFTER 2000. WHY? MANY COMPANIES ARE SO FOCUSED ON Y2K THAT THEY HAVE NOT CONSIDERED WHAT THEY NEED TO DO BEYOND Y2K.

determining whether they are focused on the right things in terms of IT's contribution to the business. There are even indications that, if this is not being done, companies are actually taking value out of the business.

Real Life

Following are actual client situations we have encountered which illustrate the value of closely integrating IT within business operations and decisions:

- An IT manager asked for help in selecting an MRP (materials requirements planning) package. The real issue/problem was that the business needed a simple work-in-process tracking tool and didn't need to invest the time, cost, and resources required for MRP at that time. A simpler solution resulted in immediate value that was significant in terms of reducing inventories and faster response to customer orders.
- A CIO wanted help in justifying an ERP decision to his CEO—only to find that not only was ERP not of the highest value to the business (it ranked eighth overall), but also he had selected the wrong ERP package because he did not clearly define the future needs of the business. The company postponed and eventually scrapped the project, which had already cost \$4.5m.
- A VP of manufacturing needed to reduce cycle time, increase productivity (to drive down product costs, yet increase product innovation), and reduce product liability. Fortunately, the CIO was progressive enough to have re-prioritized IT initiatives and investments across

the company. As a direct result, IT investments helped it gain a 90 percent market segment increase. It was focused on emerging markets as opposed to its highly competitive, low-margin markets.

- A CFO asked if the company was investing in the "right" technology by developing a \$100m logistics system. A quick analysis indicated that he was underinvesting in the critical infrastructure for the company by \$20m per year to maintain a \$280m infrastructure. That meant the \$100m system would not be sustainable with the future infrastructure and would result in extremely high replacement costs.

As you've probably noticed, these real-life situations do not speak to some emerging capabilities, such as Web strategies and e-commerce, that IT can bring to the business. Rather, these IT enablers represent real value drivers, resulting in significant competitive advantages to companies.

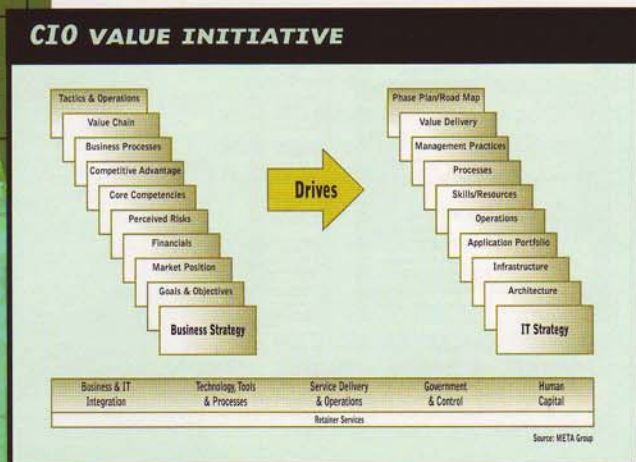
Plan Now

What are you going to do with your Y2K investment?

You have probably seen various predictions, such as 10 percent of companies will fail due to Y2K problems. Another estimates that 10 percent more will fail after 2000. Why? Many companies are so focused on Y2K (e.g., freezing IT budgets) that they have not considered what they need to do beyond Y2K. Progressive companies are planning for how to apply their investment strategically, competitively, and as a new business enabler.

Following are examples of "beyond Y2K" IT thinking which involves other views toward averting risk—and adding the most value:

- One company has a carefully planned transition underway right now. It is transitioning its Y2K program management office to a value program office, taking the "best and brightest," along with the IT information they learned in addressing Y2K issues, and applying them to the business.
- Other progressive companies have identified their critical business processes by process mapping. They are now applying measurements and what-if scenarios to determine where IT systems can add the most value. Similarly, two other companies have been able to clearly map their infrastructure value to the operations of the business. In some situations,



COMPANIES WILL BE AT RISK IF THEIR IT ORGANIZATIONS DO NOT PROACTIVELY SUPPORT BUSINESS EFFORTS. THEY MAY STILL BE ABLE TO AVERT RISKS SUCH AS Y2K, BUT THEY WILL NOT BE ABLE TO AVERT REAL RISK SUCH AS LOST CUSTOMER MIND SHARE, REDUCED SALES, AND DECREASED SHAREHOLDER VALUE.

business leaders are not only asking questions, but demanding that IT experts be added to their business process teams, such as those for re-engineering, continuous process improvement, activity-based management, and similar business initiatives.

The focus on value is complex and difficult, and most new concepts or programs are met with skepticism and even fear. However, the Value Assurance Program (see graphic) approach enables a company to measure the value that IT delivers to the business, as defined by the business, while effectively managing IT resources.

Seven basic steps are involved:

1. Gain agreement from the executive staff on a business value agenda for IT—how IT will be used, leveraged, and applied for the business.
2. Define the value leverage areas in business terms and measures so that business stakeholders can use IT and the value of information to provide new or additional leverage points.
3. Align and communicate value expectations—what IT considers to be the critical drivers and what is needed for the business, and then what the business units say they need from IT—identifying where gaps are that need to be aligned.
4. Define and agree on best actions—IT actions and capabilities that will most effectively enable the critical business processes and drive the most value.
5. Develop a value scorecard defining IT value in business terms. Begin to move from traditional measures (e.g., return on investment, internal rate of return, economic value added), which measure the “time value of money,” to more sophisticated measures of “money value of time or risk.” This helps to manage IT and information as assets.
6. Define the value initiative—the enterprise must be able to understand the initiative and relate it to its own particular business units or functions, as well as its own personal gains.
7. Implementation and measurement—although implementation is obvious, there must be a clearly defined plan, along with ongoing measurements that will validate the value of IT to the business.

As indicated, this entails a significant change in viewing IT and information. Once there is a foun-

dation of understanding and measuring value, expectations can be set, measured, and managed. A value approach provides the best tool for averting risk and maximizing the contribution of IT to the business.

The Value Equation

With a value approach, you can be more assured that your IT organization is focused on the right projects and investments to support enterprise-wide business objectives. Other benefits derived from a value program can include competitive advantage via e-commerce solutions, better customer intimacy, and improved earnings per share. As stated, risk management is only one element in the value equation. Companies will always be at risk if the IT organization does not proactively support business efforts. Technology is driving a new understanding of the business and market economy. Companies that don't recognize this fact may still be able to avert risks such as Y2K, but they will not be able to avert real risk such as lost customer mind share, reduced sales, and decreased shareholder value.

The traditional IT approach has been as follows: take the order, develop the application on time and within budget, keep the system up and running (or avert system disaster), answer to the business, and react to symptoms and squeaky wheels.

A new IT paradigm is developing: identify, quantify, measure, and maximize the value and contribution of IT to the business. Put yourself and your organization out there by leading the change in your organization—developing a value approach and becoming proactive with the business. 🖐

Ray Arpin is the vice president and practice leader of META Group Consulting's Value Performance practice. The practice is focused on Year 2000; risk management; contingency/crisis planning; project, program, and process management; IT strategy; architecture; and technology—all linked to the group's Value Assurance Program.



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