

Competence Center InfoCom

Managing the IT cost challenge



MANAGING THE IT COST CHALLENGE

I. Entering the next round of IT cost reduction

The economic downturn has forced companies to dramatically reduce their production capacity and to lay off staff in both operational and non-operational functions. This trend has also reached the IT function: CIOs are accelerating their efforts to reduce IT costs, which – depending on the industry – may account for over 10% of operating expenses. Our benchmarking experience reveals substantial differences in IT cost ratios among industry peers – in some cases beyond 30%. At the same time, IT value creation is often not fully visible to the business.

To succeed during the current economic downturn, CIOs must radically streamline the IT function. The fact that IT cost management has been an ongoing issue on CIOs' agendas will make the current IT cost reduction round even more challenging.

II. Eleven IT levers to success

Roland Berger Strategy Consultants can help its clients significantly reduce their IT costs. Experience shows that in most cases, an IT cost reduction of roughly 20-30% is feasible within 12-18 months. Our toolbox has over 100 ready-to-use IT cost reduction actions that can be grouped into eleven levers (shown in figure 1).

Figure 1: IT lever landscape

A IT MANAGEMENT AND OVERHEAD		C IT OPERATIONS AND SUPPORT	
1	Eliminate redundant IT management and overhead functions	6	Standardize IT products and services
2	Simplify commercial IT procedures	7	Industrialize IT operations and support
B IT PROJECTS AND MAINTENANCE		8	Right-size IT service levels
3	Optimize IT project portfolio management		
4	Cap IT project and maintenance budgets		
5	Optimize IT development processes		
9	Simplify IT architecture		
D IT OUTSOURCING			
10	Improve IT sourcing mix		
11	Leverage IT sourcing power		

Source: Roland Berger

Lever 1 – Eliminate redundant IT management and overhead functions

Identifying and (where possible) eliminating duplicate management and overhead functions can help avoid the costs of redundant execution and reduce the diversity of requirements and directions. Especially after M&A activities or phases of strong growth, this lever is of great importance.

Lever 2 – Simplify commercial IT procedures

As IT departments are often obliged to fulfill complex pricing and billing requirements, introducing simplified pricing rules and invoicing schemes will help realize considerable savings in terms of time and commercial workforce.

Lever 3 – Optimize IT project portfolio management

Maintaining a well-defined project portfolio management to systematically capture and assess project requests with regard to costs/benefits and associated risks tends to be an ongoing challenge. Introducing a sound mechanism helps convey a complete picture of the IT project portfolio and thus favor those projects that have a strong business case as well as a balanced risk profile. Projects with overly long payback periods or considerable risks should be skipped or at least prioritized accordingly.

Lever 4 – Cap IT project and maintenance budgets

Introducing project portfolio management usually goes hand in hand with reducing and reallocating IT project budgets. In practice, implementing these two levers often leads to an adverse effect: project requests are split into several small orders and are executed via maintenance procedures. Thus, in addition to restructuring the IT project budget, clear caps also need to be defined for maintenance procedures in order to avoid bloated IT maintenance budgets.

Lever 5 – Optimize IT development processes

To better ensure that software projects meet expectations in terms of functionality, cost and delivery schedule, it is essential to introduce a well-defined software development process that is supported by the right tools. Additionally, improving the sometimes difficult interface between business and IT helps guarantee that business requirements are met throughout the process.

Lever 6 – Standardize IT products and services

The variety of IT products and services is one key driver of operations and support complexity. Although standardization efforts may not have a positive financial impact by themselves, they usually act as door opener for other levers such as the industrialization of IT delivery processes.

Lever 7 – Industrialize IT operations and support

During the last forty years, IT has supported many industries in becoming more flexible and cost efficient. Now, decades after IT refined industrial processes, the IT community faces an increased need to industrialize the IT function itself. Building upon the standardization of the IT product and service portfolio (see lever 6), IT industrialization involves consolidating IT operations and support locations as well as introducing automated delivery processes.

Lever 8 – Right-size IT service levels

By adjusting service levels to actual business requirements, further cost savings may be achieved. Our experience shows that service levels are often unnecessarily high – and that the IT function tends to even exceed existing agreements.

Lever 9 – Simplify IT architecture

IT architecture that has developed unsystematically over time offers room for simplification, e.g. by defining architectural standards/guidelines, retiring applications and infrastructure, and improving application and data integration. This lever offers significant financial benefits. Unfortunately, the related one-time costs tend to be high as well.

Lever 10 – Improve IT sourcing mix

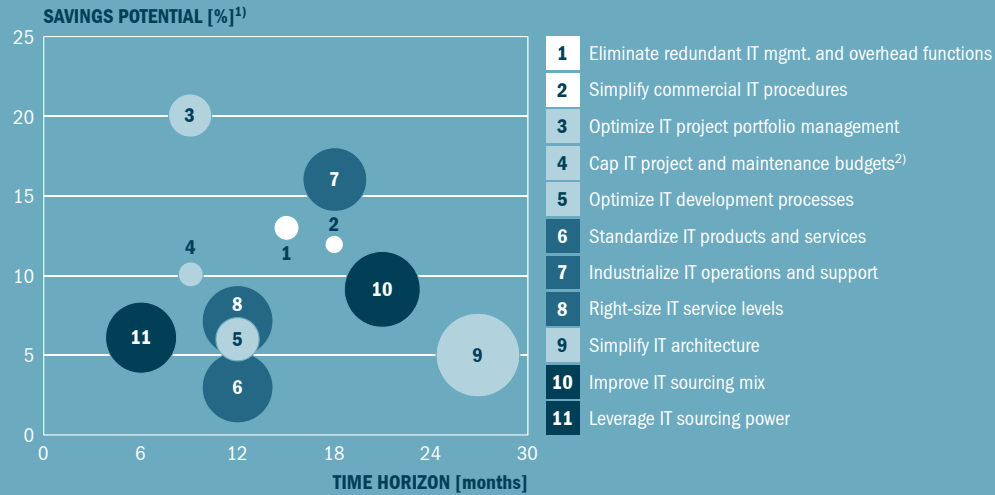
Depending on the degree of specificity and the value contribution of the particular IT service, the extent of vertical integration should be questioned. While core IT services have to be provided in-house, complete or partial outsourcing of non-core IT services should be considered in order to find the right – i.e. value-maximizing – sourcing mix.

Lever 11 – Leverage IT sourcing power

This lever aims at bundling procured IT volumes across business segments to leverage the IT sourcing power of an organization. The benefits are particularly large for all IT products and services sourced from global suppliers. As implementing structural changes to the sourcing process will take some time, renegotiating existing contracts with external hardware, software and IT service providers can help achieve quick wins without inflicting additional pain on the organization. Here, the chances of success are determined by contractual obligations, the (theoretical) opportunity to change the provider, and negotiating skills and tactics.

The levers described above differ significantly in terms of relevant cost base, savings potential and implementation time horizon (see figure 2). Typical quick wins tend to be found within IT procurement and IT project portfolio management while – for example – IT architecture-related actions require considerable up-front effort.

Figure 2: Time horizon and impact per lever



1) In percent of relevant cost base 2) Relevant cost base comprises maintenance budget only
 Note: Bubble size indicates relevant cost base, levers overlap with respect to relevant cost base
 Source: Roland Berger

III. Overcoming implementation hurdles

Running an IT cost reduction program may be considered disruptive to well established operations. The successful execution of such a program requires early identification and consideration of implementation hurdles. In our experience, two implementation hurdles deserve particular attention on the executive level:

- > Firstly, as staff-related IT costs account for roughly two thirds of total IT costs, the majority of the levers mentioned above will have an impact on headcount. While the external workforce can be reduced at short notice in most cases, options such as alternative employment, early/partial retirement or severance pay have to be considered carefully before laying off internal staff.
- > Secondly, as most levers will also have an impact on business, their implementation cannot be decided by IT management on its own. A joint effort between business and IT as well as strong business governance and support are essential for realizing the identified potential.

IV. Ensuring sustainability

The completion of an IT cost reduction program can be considered successful only if the achieved cost level proves to be sustainable. Two factors are critical to ensure this:

- > A cost reduction program must also always focus on "IT run" costs instead of only temporarily lowering "IT change" costs. Applying cost reduction actions unilaterally to the latter will inevitably lead to IT gradually becoming obsolete and producing little to no innovation with respect to business processes.
- > On the other hand, non-competitive IT costs are often the result of an overly complex IT setup. In such cases, creating a more streamlined organizational structure and governance model is essential. This may include introducing reporting lines between the various (and currently independent) IT organizations, clarifying IT decision-making rights and responsibilities company-wide and changing attitudes toward performance and competition.

V. What we can do for you

Based on our comprehensive experience in IT cost reduction and prevention, Roland Berger Strategy Consultants can identify and prioritize value-adding actions, achieve quick wins and help implement a comprehensive set of IT cost reduction activities reliably and quickly. In the process, we retain an objective position while combining business and IT staff into a single team to make the most of identified opportunities.

For further information, please contact Andreas Dietze (+49 211 4389-2192) or Stefan Hörmann (+49 89 9230-8871).

Published by Roland Berger Strategy Consultants GmbH
Dirk Reiter, Andreas Dietze
InfoCom CC
Mies-van-der-Rohe-Strasse 6
80807 München, Germany

www.rolandberger.com
e-mail: infocom@de.rolandberger.com

CONTACTS



Dirk Reiter

Member of the Executive Committee and
head of the Infocom Competence Center
Roland Berger Strategy Consultants GmbH
Mies-van-der-Rohe-Strasse 6
80807 München

Phone +49 89 9230-8138
Fax +49 89 9230-8639
E-mail dirk_reiter@de.rolandberger.com



Andreas Dietze

Partner
Roland Berger Strategy Consultants GmbH
Karl-Arnold-Platz 1
40474 Düsseldorf

Phone +49 211 4389-2192
Fax +49 211 9702-2192
E-mail andreas_dietze@de.rolandberger.com

Amsterdam
Bahrain
Barcelona
Beijing
Berlin
Brussels
Bucharest
Budapest
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Frankfurt
Hamburg
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